No. 2524

United States
Circuit Court of Appeals
For the Ninth Circuit

IDAHO-OREGON LIGHT AND POWER COMPANY, IDAHO RAILWAY, LIGHT & POWER COMPANY and O. G. F. MARKHUS, as Receiver of IDAHO RAILWAY, LIGHT & POWER COMPANY,

Appellants,

vs.

STATE BANK OF CHICAGO, BANKERS TRUST COMPANY, F. N. B. CLOSE, A. W. PRIEST, WILLIAM H. FORSTER, H. D. MILES, EDWARD J. MULLER, GEORGE E. FISHER, W. D. WILLARD, Personally and as a Bondholders Committee, W. J. FERRIS, as Receiver of IDAHO-OREGON LIGHT & POWER COMPANY, UNITED STATES OF AMERICA, IDAHO POWER & LIGHT COMPANY, GENERAL ELECTRIC COMPANY, WESTINGHOUSE ELECTRIC & MANUFACTURING COMPANY, A. H. SUNDLES and AMERICAN STEEL & WIRE COMPANY,

Appellees.

A. W. PRIEST, W. D. WILLARD, WM. H. FORSTER, H. D. MILES, EDWARD J. MULLER, GEORGE E. FISHER, D. M. LORD, JOHN R. ALLEN, W. O. CARRIER, ALLEN HOLLIS, CHARLES L. PARMELEE and CHARLES M. SMITH, Interveners, and Being a Protective Committee for the Holders of the First and Refunding Bonds of the IDAHO-OREGON LIGHT & POWER COMPANY,

Cross-Appellants,

vs.

IDAHO RAILWAY, LIGHT & POWER COMPANY, O. G. F. MARKHUS, Receiver of IDAHO RAILWAY, LIGHT & POWER COMPANY, IDAHO-OREGON LIGHT & POWER COMPANY and W. J. FERRIS, Its Receiver, BANKERS TRUST COMPANY, F. N. B. CLOSE, UNITED STATES OF AMERICA, IDAHO POWER & LIGHT COMPANY, GENERAL ELECTRIC COMPANY, WESTINGHOUSE ELECTRIC AND MANUFACTURING COMPANY, A. H. SUNDLES and AMERICAN STEEL & WIRE COMPANY,

Cross-Appellees.

BRIEF OF APPELLANTS

CAVANAH, BLAKE & MacLANE,
Solicitors for Appellants.
JOHN F. MacLANE, *of Counsel.*

Upon Appeal From the United States District Court for the District of Idaho, Southern Division.

SYMS-YORK CO., PRINTERS & BINDERS, BOISE

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& Alfred A. Fraser, *Solicitors for Appellants.*
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INDEX

AUTHORITIES CITED.

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v.

STATE BANK OF CHICAGO, et al.,

Respondents.

BRIEF OF APPELLANTS

STATEMENT OF THE CASE.

This is an appeal from a decree entered by the United States District Court for the District of Idaho, Southern Division, on the 19th day of September, 1914 (see Record, pages 155-164), upon a petition in intervention by A. W. Priest and others, individual bondholders and as a bondholders' committee (Record pp. 5-47), filed in equity suit No. 444, being a suit by the State Bank of Chicago, as Trustee, against the Idaho-Oregon Light & Power Company, and others, to foreclose a mortgage executed by the latter Company securing the bonds held by the interveners and others. (Record pp. 502-503). The decree was in favor of the interveners, and from it this appeal is prosecuted by the defendant Company (being allowed as to it merely *pro forma)* and by Idaho Railway, Light & Power Company and O. G. F. Markhus, its Receiver, who were respondents to the intervening petition (Record pp. 477-478).

To adopt for convenience the nomenclature used in the lower court, the Idaho-Oregon Light & Power Company will be hereinafter referred to as the "Power Company," the Idaho Railway, Light & Power Company will be hereinafter referred to as the "Railway Company," the appellees here may, so far as it is necessary to refer to them, be styled "Interveners," and as the Receiver of the Idaho Railway, Light & Power Company claims in no other right than that of the Railway Company, he need not be further separately mentioned.

A succinct statement of the formal proceedings of the cause is found in the stipulation on pages 502 to 514 of the Record, which, so far as deemed by the appellants material, is as follows:

> "It is stipulated between the solicitors of record of the respective parties hereto as follows:
>
> "That original bill was filed in the above entitled cause on July 7, 1913, by the State Bank of Chicago, a corporation duly organized and existing under the laws of the State of Illinois, and a citizen of the said state, and a resident of the Northern district thereof, having its principal place of business in the City of Chicago, County of Cook, State of Illinois, against Idaho-Oregon Light & Power Company, a corporation organized and existing under the laws of the State of Maine, and a citizen of said state, doing business in the States of Idaho and Oregon under and by virtue of its compliance with the laws of said states, said business consisting primarily in the

ownership and operation of hydro-electric power plants, stations, sub-stations, transmission and distribution lines in Ada, Boise, Canyon and Washington counties in the State of Idaho, and Malheur and Baker counties, in the State of Oregon; and the Bankers Trust Company, a corporation organized and existing under the laws of the State of New York, a citizen of said State and a resident of the City of New York in the Southern district of said state; and F. N. B. Close, a citizen of the State of New Jersey. That the suit is and was a suit in equity between citizens of different states, and that the amount in controversy therein exceeds the sum of $3,000.00 exclusive of interests and costs.

"That the bill was one to foreclose a mortgage upon properties of defendant, Idaho-Oregon Light & Power Company, consisting of an hydro-electric power plant with transmission lines and distribution systems in the States of Idaho and Oregon, and within the Southern Division of the District of Idaho, and in the District of Oregon, and of an uncompleted power hydro-electric development in course of construction on lands owned by the Company at the Ox Bow Bend of the Snake River in Baker County, Oregon.

"That it was alleged in the bill, and is a fact, that the said mortgage was executed and delivered by the Idaho-Oregon Light & Power Company to the State Bank of Chicago, as Trustee, on or about April 1, 1907, to secure an issue of

$7,000,000.00 first and refunding gold bonds of said Power Company, of which it was alleged bonds to the amount of $3,319,000.00 had been certified and were outstanding. That the defendants, Bankers Trust Company and F. N. B. Close, were joined as defendants as trustees under a mortgage executed by the Power Company on or about November 21, 1911, to Windsor Trust Company, a corporation and citizen of the State of New York, and Marmaduke Tilden, a citizen of the State of New Jersey, and to their successors in trust and assigns to secure an issue of $10,000,000.00 consolidated six per cent gold bonds, covering the same properties of the Power Company as the mortgage to the State Bank of Chicago, and junior to such mortgage, containing provisions for refunding of the bonds issued under the said mortgage to the State Bank of Chicago. That it was alleged in the bill, and is a fact, that Windsor Trust Company and Marmaduke Tilden had resigned as such Trustees, and defendants Bankers Trust Company and F. N. B. Close were and are their successors in trust. That it was alleged by the bill on information and belief that $1,800,000.00 par value of bonds had been certified under said consolidated mortgage, and that $1,770,000.00 of said bonds were outstanding.

* * * * *

"The cause came on for trial before the Court by consent of all parties on August 11, 1913, and

an informal notice of proposed application by A. W. Priest and others to intervene having been received by the Court, the cause was continued after the evidence was closed until the 14th day of August, 1913, on which day petition for leave to intervene was filed, and the cause was continued until August 20, 1913, when decree of foreclosure was entered. By said decree it was adjudged as follows:

" 'FIRST: That bonds to the amount of $3,319,000, were duly certified and issued under the mortgage, copy of which is attached to the Bill of Complaint herein as Exhibit "A," which is herein called the First and Refunding Mortgage, of the Idaho-Oregon Light & Power Company, hereinafter called the Power Company, and are now outstanding, of which $2,474,000 bore interest at the rate of 6% per annum and $845,000 bore interest at the rate of 5% per annum. That all of said bonds bearing interest at the rate of 6% per annum had been issued and were outstanding on April 1st, 1913; that on said last mentioned date $738,000.00 of said bonds bearing interest at the rate of 5% per annum had been issued and were outstanding and that $107,000.00 of said bonds bearing interest at the rate of 5% per annum were issued on the 24th day of April, 1913.

" 'That on April 1st, 1913, default was made in the payment of the interest coupons on all of said bonds then issued and outstanding.

* * * * *

"'NINTH: The Court retains and reserves exclusive power and jurisdiction to make such further orders as are necessary to carry out this decree and to vest title in the properties subject hereto in the purchaser or purchasers thereof, and to adjudicate claims to and ditribute any surplus proceeds arising from the sale after the satisfaction of plaintiff's said claim, and to make any further order in the premises as may be meet and just and as may be required.

"'The Court further retains and reserves exclusive jurisdiction to permit petition in intervention to be filed herein at the present or the next ensuing term, with the same effect as if this decree had not been entered, and to vacate this decree upon allowing the filing of any such petition, or to modify the decree in such manner as to afford intervenors any rights which they may establish. The Court further retains jurisdiction to make any order affecting the proceeds of sale or the distribution of such proceeds which may be equitable and just and which may be necessary to adjust any rights or equities which may be properly established in this proceeding by any bondholder or class of bondholders against any other bondholder or class of bondholders, and, to this end, the Court reserves jurisdiction to modify this decree in any manner which may be required. In order to enable the Court to do justice in the premises and to adjudicate rights to and distribute the proceeds of sale

in such manner as to do complete justice between all the parties, all proceeds of sale shall be paid into the Clerk of the Court and distributed only under the order of the Court to such bondholders as and in such proportions as the Court may adjudge them entitled, and nothing in this decree contained shall be deemed or construed to impair or limit the full and complete jurisdiction of the Court as reserved under this paragraph.'

"That, pursuant to the leave granted by the decree, the intervenors, A. W. Priest and others, filed their petition asking leave to intervene on the 30th day of August, 1913, and on the 15th day of September, 1913, lodged a proposed answer to the Bill of Foreclosure, and on the 17th day of September, 1913, lodged their proposed bill in intervention, making the plaintiff, the defendant Idaho-Oregon Light & Power Company, and the Idaho Railway Light & Power Company, a Maine corporation and citizen of the State of Maine, respondents to said bill, and also presented a motion to vacate the decree as entered on August 20, 1913.

"On the 19th day of September, 1913, the Court refused to permit the filing of the proposed answer, denied the motion to vacate the decree of foreclosure, but permitted the bill in intervention to be filed, and ordered issues framed thereon.

"That, in due course, and within the time allowed by Court, the respondents to the bill in intervention filed their answers thereto in accord-

ance with the directions contained in the Court's order.

"That on, to-wit, December 10, 1913, pursuant to motion of the intervenors made on or about October 15, 1913, and pursuant to stipulation of all parties to the cause, filed on December 8, 1913, W. J. Ferris was appointed Receiver of all properties of defendant, Idaho-Oregon Light & Power Company, and is such Receiver."

The cause came on regularly for trial in June, 1914, on the issues framed on the Bill in Intervention, and on August 24, 1914, the Court rendered a preliminary decision and on September 18, 1914, a supplemental decision, which decisions are shown on pages 131 to 154 inclusive of the Record, and on September 19th there was filed the decree shown on pages 155 to 164 inclusive, from which this appeal has been taken.

Some particular reference to the pleadings and the decree should be made before discussing the facts, ~~which can more appropriately be done in connection with the argument~~.

The Bill in Intervention is voluminous. After stating the formal proceedings in the principal cause and the status of Interveners as individual bondholders and as a protective committee representing other bondholders, the bill proceeds to set forth the organization of the Power Company, the reputed value of its properties, its advertised financial prospects and its management, and in paragraph V, on page nine, alleged that for the purpose of obtaining

additional money with which to complete its power development, the Ox Bow Plant, it "entered into a contract with Kissel-Kinnicutt & Company, a co-partnership engaged in the banking and brokerage business, and being members of the stock exchange of the City of New York," under which contract they were informed and believed Kissel-Kinnicutt & Company (who may be hereafter referred to for convenience as the "Bankers") were bound to purchase $1,500,000 of the issue of "Consolidated Bonds," secured by the junior mortgage to the Bankers Trust Company and F. N. B. Close, and that in addition to the purchase of the bonds, the Bankers received a large stock bonus sufficient to give them an equal voting power with the former managers of the Company, the Messrs. Mainland.

It is further alleged (p. 10), that upon acquiring control of the Company, the Bankers caused to be organized the Railway Company, with an authorized capital of $30,000,000, and executed a mortgage to secure an authorized issue of a like amount of bonds. They then (p. 11) transferred and induced the Messrs. Mainland to transfer their combined holdings in the Power Company, being a total of 77,650 shares out of an authorized issue of 100,000, to the Railway Company; caused persons of their selection to be elected officers and directors of both companies, and effecting a substantial physical consolidation of their properties, the Railway Company having acquired (p. 12) other power properties and electric railroad properties in the same district which the Power Company was serving.

In paragraph VI (pp. 12 to 13), it is alleged in substance that the Railway Company diverted business from the Power Company and threatened the latter with competition in its markets, and generally manipulated the Power Company in the interests of the Railway Company. Paragraph VII (pp. 14 and 15), alleges in substance that the Railway Company was not a profitable enterprise; that it had issued $6,500,000 of bonds, which its sponsors, the Bankers, were unable to market, and that they therefore devised the plan of foreclosing the mortgage on the Power Company's properties, and, by a proposed reorganization scheme, subordinating the bonds secured by the mortgage to the plaintiff, to those issued by the Railway Company the lien of which would be extended over the properties of the Power Company. Mismanagement of the Power Company by the Railway Company interests is further alleged in paragraphs VIII and IX (pp. 16 to 19), and paragraph X (pp. 19-27) purports to set forth the proposed reorganization scheme of the so-called Railway Interests. The remaining paragraphs contain similar allegations as to the general turpitude of the Railway management and reiterate and amplify the charges of fraud and mismanagement made throughout the bill.

Paragraph XII on pages 28 and 29 is that upon which the issues were framed, and is as follows:

> "The interveners further show that the Railway Company was sometime in the early part of 1913 in possession and claiming the ownership of

certain consolidated or second mortgage bonds of the Power Company; that thereupon the Railway Company demanded of the Power Company that it receive back these consolidated or second mortgage bonds and deliver to the Railway Company instead an equal amount of the first mortgage bonds of the Power Company, being a part of the $3,319,000.00 of bonds alleged to be outstanding and upon which foreclosure is sought in this suit; that the Power Company, being as above shown fully under the control and domination of the Railway Company, necessarily acceded and did accede to this demand, and thereupon delivered and turned over to the Railway Company $718,-000.00 of the said first mortgage bonds, after the Railway Company had collected the November, 1912, interest on the consolidated bonds. The interveners charge that the said consolidated bonds, in view of the alleged deficit in the earnings of the Power Company for the year 1912 and in view of the default and foreclosure then planned and anticipated, had no market value and were to all intents and purposes worthless, and that the said exchange of bonds was wholly without consideration and was, as to the interveners and the Power Company, wrongful and fraudulent, and that the said bonds are not, because of said issue and delivery by the Power Company to the Railway Company, issued and outstanding and valid obligations of the Power Company, but that the same should be by this Court called in and cancelled."

The prayer for relief (pp. 43-46) is for the appointment of a Receiver for the purpose of removing the property of the Power Company from the possession and control of the Railway Company, and to enforce and obtain accountings against persons and corporations who had obtained possession and control of the bonds, moneys and other property of the Power Company, including the collection and recovery of unpaid stock; that creditors be required to present and establish their claims; that if necessary the plants and properties of the Power Company be sold, etc. A supplemental prayer was added (p. 49), that the Court annul and declare illegal and void the 718 bonds obtained by the Railway Company in exchange for consolidated bonds, and that the Railway Company be made defendant to answer those allegations. A tenth clause asks (p. 50) that the decree of foreclosure and sale be vacated and set aside.

The order framing the issues appears on pages 55 to 59 of the Record. By it the Interveners were permitted to appear, and their Bill was filed, and both the Railway and Power Companies were required to answer the allegations respecting the 718 bonds, and subpoena was directed to issue to the Railway Company. The Power Company was required to answer certain other issues, viz: As to the location of 107 bonds, and of another 520 bonds, and also as to an alleged payment of interest on the April 1st, 1914, coupons. The decree, however, was favorable to the Power Company, as to the 107 bonds (Record p. 157), and the other issues mentioned in

the order, were dismissed from the case by stipulation at the opening of the hearing (Record p. 168), leaving only the issue as to the 718 bonds for determination here. None of the issues of fraud and mismanagement were required to be answered and the same were in effect dismissed from consideration (Record p. 167). The order provided (p. 57) that "the failure of any party to answer any averments of the Bill in Intervention not expressly required by this order to be answered shall not be construed as an implied admission that the same are true."

The answers of the Railway and Power Companies as to the 718 bonds, are substantially the same. Quoting from the answer of the Railway Company, after denying the allegations of the Interveners, it is alleged (Record pp. 98-101):

> "That on and prior to September 25th, 1912, the defendant Power Company was in need of $250,000.00 for its general corporate purposes and legitimate capital expenditures; that on and prior to said date, the defendant Power Company applied to the Railway Company for a loan of $250,000.00 in cash; that the Railway Company was at the time of such application the owner by purchase of consolidated bonds of the Power Company of the face and par value of about $1,500,000, which said bonds bore interest at the rate of six per cent per annum but were inferior in lien to the said refunding bonds, which said bonds bore interest at the rate of five per cent per annum; that the Power Company represent-

ed at that time that it had certified and in its treasury as free assets, refunding bonds to the amount of $305,000 and that it was entitled under the terms of its trust deed to a further issue of refunding bonds to reimburse it for expenditures made to an amount in excess of $500,000. That the Railway Company stipulated as a condition of making said loan to the Power Company that the Power Company should exchange its said first or refunding mortgage bonds then in its treasury or to which it should be entitled, to the extent of $500,000.00 for a like amount of consolidated bonds held by the Railway Company, and that it should further secure the Railway Company for loans made by it to the extent of $250,000.00 by a pledge of said refunding bonds in the ratio of two dollars in bonds for one dollar of loan; that these terms were accepted by the Power Company and an agreement for such exchange was made, a copy of which agreement is attached as Exhibit B to the answer of the defendant Power Company, which said exhibit is hereby referred to and by reference made a part hereof. That the Power Company thereupon procured the certification of the bonds to which it was entitled from the plaintiff herein as its Trustee, as hereinbefore stated, and refunding bonds to the extent of about $440,000 were exchanged by the Power Company for consolidated bonds held by the Railway Company on or about December 27th, 1912, said bonds having been theretofore delivered by the Power Company to the

Railway Company as collateral and the Railway Company accepted consolidated bonds as said collateral in lieu of said refunding bonds.

"2. That on or about the date of said last exchange, to-wit: December 27th, 1912, the Power Company applied to the Railway Company to assist it in a settlement of a controversy with the Bates & Rogers Construction Company, an Illinois corporation, hereinafter called Construction Company, and the Railway Company to assist the Power Company pursuant to said application agreed to deliver fifty shares of its preferred stock and one hundred shares of its common stock to the Construction Company and further agreed to purchase from the Construction Company on demand within a specified period $25,000 face and par value of the Power Company's consolidated bonds at eighty per centum of the face and par value thereof and interest accrued and unpaid thereon, which said bonds were then delivered by the Power Company to the Construction Company as part of said settlement of controversy. That as consideration for said agreement, on the part of the Railway Company and of its assistance in effecting said settlement, the Power Company agreed to exchange with the Railway Company additional refunding bonds not to exceed $500,000 face and par value thereof for a like amount of consolidated bonds still held by the Railway Company. A copy of said agreement is annexed to the answer of the de-

fendant Power Company marked Exhibit C and is referred to and by way of reference made part hereof.

"3. That pursuant to said agreements of September 25th and December 27th, 1912, the Railway Company duly performed all the conditions of said agreements by it to be performed and loaned to the Power Company $250,000 in cash and delivered to the Power Company from time to time, the last delivery being made in January 1913, its consolidated six per cent second mortgage bonds for refunding five per cent first mortgage bonds, which the Power Company delivered to the Railway Company and the Railway Company likewise accepted from the Power Company as collateral for its said loan consolidated bonds in lieu of said refunding bonds to which it was entitled under said agreement of September 25th, 1912. That said agreements, and each of them, have been duly performed and executed and the Railway Company claims to own and does own the said $718,000 face and par value of first and refunding bonds of the Power Company and is entitled to participate in the distribution of the proceeds of any sale in this cause to the extent thereof.

"4. This Railway Company does not admit any of the allegations of the said bill in intervention not herein denied or referred to, but limits its answer to the matters herein stated on the ground and for the reason solely that it is not

required but is expressly excused from answering the same by said order of September 19th, 1913, pursuant to which this said answer is made."

The agreements referred to in the Railway Company's answer, under which the exchanges of bonds were made, are contained at pages 112 to 123 inclusive of the Record.

The evidence introduced upon the trial was quite voluminous, but the greater part of it was record evidence consisting of exhibits, and the facts, omitting further than to mention points of conflict, may be summarized as follows:

A brief history of the organization of the Power and Railway Companies and the relations between the two, as shown (Record pp. 197, 198) by the testimony of O. G. F. Markhus, is as follows:

"Witness was General Manager of the Power Company from 1907 to and including practically the whole year of 1913. That Company became an operating Company in October 1908. Prior to that time it had commenced construction of the Ox Bow plant, and it then took over the operation of previously existing companies, known as Capital Electric Light, Motor & Gas Company, Boise-Payette Electric Power Company, Electric Power Company, Limited, Interstate Light & Water Company, and became an operating Company or distributor of electric current.

"Kissel, Kinnicutt & Company first became interested in the property or securities of the Power Company in September, 1911, and persons designated by it commenced to participate in the management of the Power Company on December 1, 1911. Prior to that time William & S. Mainland of Oshkosh, Wisconsin, were the general operators of the property; they were replaced by Mr. Watson at the instance of the new interests, represented by Kissel, Kinnicutt & Company, but the Messrs. Mainland still remained directors of the Company and members of its Executive Committee, and Mr. William Mainland continued to be its President.

"The Railway Company was organized in November 1911, and commenced business December 1, 1911, on or about which date it acquired the properties of the Swan Falls Power Company which owned a power plant at Swan Falls on the Snake River and transmission lines into the Silver City District, so-called, serving lines around Silver City and at Dewey and Murphy, and a transmission line from Swan Falls station through Nampa and Caldwell, where it was wholesaling power and from which it retailed power at Middleton; the Dewey Electric Company which distributed light and power to Nampa, the Boise Valley Railway Company, which had a railway system extending from Boise to Nampa, and the Boise & Interurban Railway Company, which had a railway from Boise to

Caldwell, and the Caldwell Power Company, which distributed power at Caldwell, Idaho."

The general situation and relations between the companies and their territory is shown by the map on page 199, which, as shown in the record, is not particularly illuminating, because of the absence of different colored lines to represent the two companies. Generally speaking it may be said that the Railway Company supplied the territory due West and South of Boise, while the Power Company served Boise and the territory North of a line which might be drawn through the Town of Caldwell, the power lines coming in contact near Boise.

Immediately upon its organization in 1907 the Power Company created the mortgage foreclosed in this suit, material parts of which are quoted on the record from pages 383 to 396 inclusive. The mortgage was the usual form of corporate mortgage to secure an issue of bonds of $7,000,000, the bonds reciting (Record p. 384) "the payment of all of which bonds, with interest as aforesaid, is equally and ratably, and without preference of one bond over another, secured" by the mortgage to plaintiff. Later in the bond followed the clause (pp. 384, 385):

"The holder of this bond shall have no recourse for the payment thereof or of any coupons issued therewith or of the indebtedness thereby evidenced, to any individual liability of any incorporator or any past, present or future stockholder, officer or director of the undersigned, im-

posed by any statute or otherwise or for or on account of anything or act heretofore or hereby done or omitted, all such liability being taken to be waived by such holder at the time of the purchase hereof, and by accepting this bond each successive holder assents to the terms of this provision.

"This bond shall not become obligatory until it shall have been authenticated by the certificate of the said State Bank of Chicago, as Trustee endorsed hereon."

After the granting clause and the description of the property appears the following (Record p. 386):

"IN TRUST, HOWEVER, for the equal and proportionate benefit and security of all present and future holders of the bonds and coupons issued and to be issued under and secured by this indenture, and for the enforcement of the payment of said bonds and coupons, when payable, and the performance of and compliance with the covenants and conditions of this indenture, without preference, priority or distinction, as to lien or otherwise, of any one bond over any other bond by reason of priority in the issue or negotiation thereof, so that each and every bond issued and to be issued as aforesaid shall have the same right, lien and privilege under this indenture, and so that the principal and interest of every such bond shall, subject to the terms hereof, be equally and proportion-

ately secured hereby, as if all had been made, executed, delivered and negotiated simultaneously with the execution and delivery of this indenture; it being intended that the lien and security of this indenture shall take effect from the day of the date hereof, without regard to the date of actual issue, sale or disposition of said bonds, and as though upon the day of such date all of said bonds had been actually issued, sold and delivered to, and were in the hands of innocent holders for value."

By Article 2 the purposes for which the bonds may be used are set forth. (Pages 387-393). Without quoting them in detail it is provided briefly that bonds numbered 1 to 500, inclusive, should be immediately delivered to or upon order of the President of the company. Bonds 2501 to 3050, inclusive, should be set apart for the purpose of retiring outstanding underlying divisional bonds. Bonds 501 to 2500 should be certified and delivered to the trustee from time to time for the purpose of building the Ox Bow Power plant on the Snake River, it being provided that the bonds should only be delivered "in the proportion that the work then done and material then purchased bears to the said $2,000,000 of said bonds," the purpose being to insure the completion of the plant within the amount limited therefor. The remainder of the bonds, Numbers 3051 to 7000, inclusive, were required to be held by the trustee until certified and delivered by it to the company for one of the following purposes.

"(1) To provide means for the purchase or acquisition of other properties or plants of a kindred character." (Page 390.)

"(2) For the purpose of retiring bonds or other evidences of indebtedness against properties thus acquired. (Pages 391, 392.)

"(3) For ninety per cent of such amounts as may be after this date actually expended by the said Company in additions, improvements, extensions, enlargements, equipments, or betterments to any of its plants or property now or hereafter acquired." (Page 393.)

During the course of the trial the following was stipulated. (Record pp. 378, 379.)

1. That the total amount of first mortgage bonds in the treasury of the Idaho-Oregon Light & Power Company on September 25, 1912, plus certifications subsequent to September 25, 1912, and prior to April 1, 1913, was $718,000, all being five per cent bonds.

2. That the total amount of Idaho-Oregon bonds certified subsequent to April 1, 1913, was $107,000, five per cent bonds.

3. That the total amount of bonds outstanding certified under the mortgage to the State Bank, the complainant herein, prior to September 25, 1912, was $2,494,000.

4. That the Idaho-Oregon Company began shortly after its organization the construction of the so-called Ox Bow plant, at the Ox Bow bend of the Snake

River, on the border of Idaho and Oregon, and up to May, 1910, the company had expended, according to its records, approximately $2,000,000 upon the construction of said Ox Bow plant and the transmission line to connect the same with the company's distributing system. That the company then had legal advice that further issues under the mortgage of the State Bank of Chicago, complainant herein, could not be used for completing the Ox Bow. On September 19, 1911, this plant remained uncompleted, no part of it being in operation, and no power being produced thereat.

It was further stipulated (Record pp. 396-398):

The requisitions by the Company to the Trustee for the bonds which are included within the 718 bonds now held and claimed by Idaho Railway Light & Power Company and its receiver were for the following numbered bonds which were received by the Company and were made between the dates, and to fund expenditures made by the Idaho-Oregon Light & Power Company shortly preceding those dates, for the purposes stated.

1. Bonds 2501 to 2540 to reimburse the Company for expenditures made in retiring the underlying divisional bonds on the properties formerly belonging to the Electric Power Company, Limited, but at the time of such expenditure and now belonging to the Idaho-Oregon Light & Power Company, and covered by the mortgage to the plaintiff, State Bank of Chicago. Of said bonds the Railway Company holds numbers 2501 to 2514, inclusive, and 2525 to 2534

inclusive, aggregating $24,000.00, and representing the number of Electric Power Company bonds actually retired, the remaining sixteen of said bonds not having been retired, and the sixteen bonds requisitioned for such retirement not having been used, and not being within the bonds held or claimed by the Railway Company in this case. These bonds were requisitioned and received by the Company during the month of April, 1909.

2. Bonds numbered 3051 to 3288, inclusive, requisitioned and received by the Company between April 1, 1908, and August 20, 1910, to reimburse the Company for 90 per cent of such amounts as had actually been expended by the Company since, to-wit, January 1, 1908, in extensions, enlargements, equipments or betterments to its plants and property, as provided in paragraph 3 of Article 2 of the mortgage.

3. Bonds No. 3289 to 3341 requisitioned and received by the Company between September 1, 1909, and November 1, 1910, to reimburse the Company for expenditures made in the purchase by it during said period or prior thereto, and subsequent to January 1, 1908, of (a) The Emmett lighting plant and distributing system, (b) The Payette lighting plant and distributing system, (c) The Interstate Lighting plant at Ontario, Oregon, all of said plants then and now belonging to said company.

In connection with these expenditures and the bonds issued to reimburse the company therefor the

following statement by the company's manager is of importance: (Record p. 432.)

During the years 1908 to 1912 inclusive the Power Company had no other source of income or revenue from which expenditures could be made in retiring underlying bonds, purchasing properties or making additions, enlargements, etc., to its plants and properties than the earnings and proceeds of second mortgage bonds, where the expenditures were not originally made in the first instance from the proceeds of the first mortgage bonds.

What has gone before is regarded by appellants as so material to their case that it has been inserted for the convenience of the Court at length.

Turning now to the facts having immediate bearing on the transaction in controversy we find that on the 19th day of September, 1911, the Power Company, its managers and principal stockholders, the Messrs. Mainland, and the Bankers, Kissel, Kinni-

mon form of underwriting contract, and, in view of the large commitment involved and the speculative

inclusive, aggregating $24,000.00, and representing the number of Electric Power Company bonds actually retired, the remaining sixteen of said bonds not having been retired, and the sixteen bonds requisitioned for such retirement not having been used, and not being within the bonds held or claimed by the Railway Company in this case. These bonds were requisitioned and received by the Company during the month of April, 1909.

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3. Bonds No. 3289 to 3341 requisitioned and re-

4. Bonds No. 3342 to 3754 requsitioned September 25, 1912, and received by the Company during December, 1912, and January, 1913, to reimburse the company for ninety per cent of expenditures made under said Clause 3 of Article 2 of the mortgage for ninety per cent of such amounts as had been expended between July 1, 1910, and July 31, 1912, in additions, improvements, extensions, etc., to the Company's plants and properties.

In connection with these expenditures and the bonds issued to reimburse the company therefor the

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What has gone before is regarded by appellants as so material to their case that it has been inserted for the convenience of the Court at length.

Turning now to the facts having immediate bearing on the transaction in controversy we find that on the 19th day of September, 1911, the Power Company, its managers and principal stockholders, the Messrs. Mainland, and the Bankers, Kissel, Kinnicutt & Company, entered into a contract, (Record pp. 168-193), by which the Bankers agreed, under certain conditions, to purchase $1,500,000 face value of the consolidated, or, as they are generally referred to in the ~~mortgage~~ record, second mortgage bonds of the Power Company, at the price of eighty hundred dollars per bond, and received as consideration therefor a large quantity of stock of the Power Company so as to give them an equal voice with the Mainlands in its management and control. The contract was a very common form of underwriting contract, and, in view of the large commitment involved and the speculative

character of the securities purchased, it gave the Bankers large control of the financial policies of the Power Company although such control was really only equal to that of the Messrs. Mainland. The contract is also of interest in that it contemplated the independent purchase of the Swan Falls Power properties and contains provisions for the organization of a new Company to hold the title to those properties, and for the consolidation of the interests of the two companies. (Pages 182-187).

The manner in which the Bankers became introduced to the properties of the Power Company and interested in them is briefly explained on pages 194 and 195 of the Record, and, on the latter page, after stating that a syndicate was formed to take over the Bankers' holdings in the Power Company and in other properties which they had acquired, and which later became the properties of the Railway Company, Mr. Fuller, the snydicate manager, stated:

> "The syndicate found itself owning a large interest in the Idaho-Oregon Company, and also, for the benefit of the Idaho-Oregon Company and for the benefit of the entire situation it had built up here an absolutely independent and self-sustaining and what was going to be a profitable enterprise, consisting of a power plant, and a large interurban and urban street railway system, and they therefore, as the Idaho-Oregon Company was in no position financially to take over the properties of the Railway Company, and the syndicate had two interests, thought it would

be wise to turn over all of their interests in the Idaho-Oregon Company to the Idaho Railway Company, which they did, taking securities of the same class from the Idaho Railway for securities of the Idaho-Oregon Company, which they turned in to the Railway Company. In order to protect the stockholders of the Idaho-Oregon Company who had a security of questionable value in the stock of the Idaho-Oregon Company, opportunity was voluntarily given them by the Idaho Railway Company to exchange their securities in the Idaho-Oregon Company for securities in the Idaho Railway Company. A circular was sent out to all the stockholders of record, and a very large proportion of the stockholders so exchanged their stock; in that way all of our interests, our stock interests were in the Idaho Railway Company, which in turn controlled the Idaho-Oregon Company."

The syndicate operations continued for about a year during which the Railway Company was in its formative period, and acquired the properties hereinbefore mentioned. The latter part of August or early in September, 1912, it clearly appears that for various reasons the enterprise of the Power Company, at least, and, the interveners will contend (which we do not think was true, and if true we regard as immaterial) the Railway Company, was not prospering as had been anticipated. The reasons for this may be the occasion of comment and dispute during the argument. It will be enough at this time to

call attention to interveners exhibits 30 and 31 (Record pp. 220, 224), being report showing results of operation and general balance sheet of the Power Company for September, 1912. It there appears that the net earnings of the Power Company available for fixed charges for the first nine months of 1912 were $175,598.79. That the total of fixed charges including the item "contingent interest," which is explained in Note (A) on page 221, exceeded that amount by $36,655.33, which represented a deficit then facing the Company. It further appeared that the net earnings of the Company had decreased over those of the previous year by sixteen and two-tenths per cent. (The Exhibit is a little obscure in that it fails to print deficits in red as shown on the original exhibit, but whether surplus or deficit is indicated will readily appear from a subtraction of the figures, giving the result.) It further appeared that the Company had, on August 31st, but $49,420.59, cash on hand. That it had accrued bond interest of $110,-266.65, and accounts payable of $80,078.20. That the Company could not continue to operate profitably or at all and meet its obligations was apparent.

By way of parenthesis it may be observed here, so that the matter may be disposed of, that the difference between the showing of the Company December 31, 1912, exhibiting a deficit of $59,654.28, as compared to a profit shown in the audits of $146,532.54 for the preceding year, and an equally favorable showing for years prior to that, which is alleged in the Bill of Intervention in support of the charges of

mismanagement, is explained by the auditors (Record p. 436), as follows:

> "Results for the year ending December 31, 1912, after providing for interest on bonded and floating indebtedness, but subject to the qualifications made in the preceding paragraph, show a loss of $59,654.28, as compared with a profit of $146,532.54 for the year ending December 31, 1911. This unfavorable showing is largely due to the fact that in 1912 there has been deducted the sum of $133,443.90 in respect of interest on bonds issued in connection with the Ox Bow construction, all interest on these bonds having been previously charged to capital."

Further, with respect to increases of operating expenses, we call attention to the following from the auditor's report (Record p. 435):

> "Included under the heading of operating plants at Boise and other points is an account of development amounting to $32,696.52, representing charges for advertising, management, salaries, canvassing, soliciting, etc., to December 31, 1910. Similar expenses aggregating $23,339.80 were charged to this account during the year 1911 by the company's officials, but we have treated these charges as operating expenses in this report, as we are of the opinion that the Company had, on December 31, 1910, arrived at a point where such charges could no longer be regarded as capital expenditure."

The balance of the increase in operating expense is explained by the increase in purchase power charge as shown on Exhibit 30 above mentioned (p. 220), which, for the first nine months of 1912, was $26,863.46, as against $212.61 for 1911, due to the growing demands on the Power Company's system and the inadequacy of its power supply.

We do not regard these points as of importance, except as explaining the prejudicial inference which might otherwise be drawn against the new management for the very unfavorable showing of 1912 as compared with 1911, and we do not desire to again refer to it.

It will thus be observed that there was no prospect of the Power Company then meeting the accruing installment of the interest upon the consolidated bonds, which the Bankers had purchased and delivered to the Railway Company in exchange for its securities. But this was not all. The record shows (pp. 431, 432) that a new element had entered into the situation since the Fall of 1911.

> "A Company known as the Beaver River Power Company obtained a franchise in Boise in February or March, 1912, and built its transmission lines to Boise City. Commencing the first part of July in that year, and continuing for several months, the Company solicited business in Boise City, the principal work being done in July and August. At the time the base rate of the Idaho-Oregon Light & Power Company was 15c per kilowatt hour with a 10% discount for

prompt payment. For larger quantities of current the rates were somewhat less, there being a sliding scale depending upon the amount used. The advertised and solicited rates of the Beaver River Power Company during that time were 9c per kilowatt hour net as a base rate, with proportionately lower rates following the same general curve rates as the Idaho-Oregon Company. This Beaver River Company installed a distributing system in Boise during 1912, and commenced actual service of current in December, 1912, from a power plant owned by that Company."

The immediate capital requirements of the Company on September 1, 1912, are shown by respondents Exhibit F (Record pp. 426, 429), showing that for the four remaining months of the year, or to December 31, 1912, the Company, in addition to all its estimated income and revenue needed for that period $203,180.

This matter was considered at a meeting of the Executive Committee of the Company on August 30, 1912, (Record p. 232), where the following occurred:

"The question of raising additional funds for the Idaho-Oregon Light & Power Company to take care of the extension of distributing systems and the building of transmission lines was taken up and discussed, and on motion of Mr. Watson, seconded by Mr. Mainland, it was

"Resolved, that a statement should be prepared and submitted by Mr. Markhus, as general man-

ager of the Idaho-Oregon, showing the expenditures that had been made by that company in connection with the building of transmission lines, sub-stations, and distributing systems since July 1, 1910, and that the same should be forwarded to the Board of Directors for approval, for the purpose of being filed with the trustee under the mortgage, so that additional bonds may be secured for the raising of funds."

At this time the Bankers had purchased from the Company $1,325,000 of the consolidated bonds which they were required to purchase by the contract of September, 1911, and were still obligated to purchase $175,000 of those bonds, which would have yielded $140,000 cash. (Record p. 237). The question of the future of the Company came up at a director's meeting held in New York City on September 25, 1912, shortly following the meeting of the Executive Committee at Boise on August 30th. The minutes of this meeting are set out at pages 233 to 250. Eight directors were present out of the total of eleven, as shown on page 233. The material part of these Minutes are on Pages 236 to 245, inclusive. Among other things the following appears:

"Mr. Watson made a statement as to the financial condition of the Company, and in conclusion recommended the raising of the sum of two hundred and fifty thousand dollars ($250,000) to meet the requirements of the Company for the next seven months.

"The Chairman presented and read to the meeting an agreement which Messrs. Kissel, Kinnicutt & Co., and Messrs. Wm. & S. Mainland proposed to make with this Company covering the loan to this Company of the sum of two hundred and fifty thousand dollars ($250,000) as above mentioned."

The Agreement recited the fact that Kissel, Kinnicutt & Company were further obligated to buy $175,000 of the consolidated bonds to yield $140,000, but were not willing to advance any more money, and therefore, in consideration of releasing them from the obligation to buy the consolidated bonds they agreed to procure the Railway Company to loan to the Power Company the sum of $250,000, which it was recited was required by it, but should receive as collateral for such loan its first mortgage bonds in the ratio of $2.00 per bond for $1.00 of loan, and should likewise have the privilege of exchanging not to exceed $500,000 of the consolidated bonds, which had been purchased for a like amount of the First and Refunding Bonds secured by the mortgage to plaintiff, as a bonus or premium for making the loan. After reciting the agreement, the minutes continue as follows: (Record p. 242.)

"After a discussion of said agreement, on motion duly made and seconded, the following resolution was unanimously adopted, with the exception of Mr. Fuller's and Mr. Sinclair Mainland's votes which were not cast:

"RESOLVED, that the agreement so presented and read to the meeting, be, and the same hereby is, in all respects, confirmed, ratified and approved, and that the proper officers of the Company be, and they hereby are authorized and requested to execute said agreement in the name of this Company and in its behalf, and to exchange the same when executed with Messrs. Kissel, Kinnicutt & Co., and Messrs. Wm. & S. Mainland.

"The Chairman thereupon presented and read to the meeting a proposal from Idaho Railway Light & Power Company to advance to this Company the sum of two hundred and fifty thousand dollars ($250,000), which proposal was as follows:"

Then follows the Railway Company's proposal in accordance with the offer of Kissel, Kinnicutt & Company, and on Page 245, at the conclusion of such proposal, the following:

"RESOLVED that the offer of Idaho Railway Light & Power Company so presented to this meeting, be, and the same hereby is, accepted, and that the proper officers of this Company be, and they hereby are, authorized and directed to do all such things as may be requisite and necessary to close said loan."

There is considerable testimony in the record as to what took place at this meeting. It is not disputed that the transactions did take place as recorded in

the minutes, but it is contended, and there is evidence in support of the contention, that of the eight directors, for one reason and another, only four voted affirmatively for the first proposition of releasing the Bankers from their obligation. It is undisputed, however, that, as to the proposition of the Railway Company making the loan, there were no dissenting votes, and the contract was executed as authorized. We do not cite the record in detail as to these disputes, because in the view we take of the case they are not material. Generally, as typical of the testimony on this subject we refer to Record pages 290-302, 309-313, as introduced by interveners; 272-277 as introduced by respondents; 285-287 introduced by interveners, but favorable to respondents.

With respect to transactions had under this contract, the witness, G. E. Hendee, Secretary of both companies, stated, (Record, p. 258):

> "The loans provided for at that meeting in connection with the exchange of consolidated for refunding bonds were made to the Power Company as follows:
>
> "October 4, 1912, $100,000.00; November 1, 1912, $20,000.00; December 11, 1912, $60,000.00; December 17, 1912, $40,000.00; January 3, 1913, $30,000.00, and continued: '440,000 first and refunding Idaho-Oregon five per cent bonds were put up as collateral against this loan, and such bonds were exchanged bond for bond for a like number of consolidated six per cent bonds previously held by the Railway Company,

> the Railway Company taking consolidated six per cent bonds as collateral for the loans when such exchanges were made.' "

This was the first transaction covered by the testimony. The reasons given for it may be inferred from the testimony hereinbefore referred to as to the financial requirements and future perils of the Company through competition, and were the obvious ones of the necessity of keeping the Company going, at least until its future could be determined with some certainty. Thus the managing director, Mr Watson, stated (Record p. 275):

> "There was a great deal of uncertainty at that time as to what our future was to be—you know what I am referring to. Q. Uncertainty in what respects? A. Uncertainty in connection with competition was staring us in the face. Q. Did you feel that there was uncertainty about the Company being unable to keep on going? A. In view of the competition. Q. In view of everything? A. In view of everything, yes."

So Mr. Wiggin, a Director of the Company and called by interveners, stated (Record p. 286):

> " 'My understanding as to the need of money was it was simply to keep the Company going.' 'It was represented to us that we just had to have money, that they needed it and it was urgent.' 'I understand that part of it was for debts already incurred.' 'We understood they needed the money, and that if they didn't get the money

they would fail.' 'Q. Fail at once? A. Yes but I don't know for how long a time, nor they didn't say how much would put them on a financial footing. It seemed to be the wise thing to do at the moment to give them money and keep them from failing.' "

That the Company was badly in need of money was admitted by all the witnesses. Thus, at page 311, Mr. William Mainland, one of the principal witnesses for interveners, stated:

"Mr. Markhus, as Manager of the Company got up the statement referred to in the minutes, but he did not recall that it had been sent to him prior to September 25, 1912, nor had it ever been received or considered by him or by the Executive Committee up to that date. From the witness' view point this two hundred fifty thousand dollars was not sufficient to meet the Company's requirements, or put it on a secure basis, his contention being that the Company needed additional power, and that sum was not sufficient to produce it. He did not recall any specific statement as to what should be done with the $250,000, except that it was for general corporate purposes, some of the money having already been spent. The statement was not sent to him as President of the Company because all communications, unless otherwise instructed, were sent by Mr. Markhus to Mr. Watson."

Also Mr. Sinclair Mainland, for the interveners, stated (pp. 322, 323):

"He knew the Company was in need of funds at the time, and the question of financial needs had been a matter of frequent discussion between the responsible officers of the Company. 'It is a matter of frequent discussion, I believe, in every business, including the New York Central, that they need further funds for their business, and probably we discussed the need of funds when we met.' "

As to the second transaction mentioned in the Railway Company's answer, there was introduced in evidence, as respondents' Exhibit B, minutes of a meeting of the Executive Committee of the Power Company held in New York on December 27, 1912 (Record pp. 400-413). It appears from these minutes that there had been a controversy between the Power Company and the Bates & Rogers Construction Company, and that to assist in the settlement of the controversy the Railway Company had agreed to give the Construction Company one-hundred shares of its common stock, fifty shares of its preferred stock, and to, in effect, guarantee at eighty per cent of their par value, $25,000 face value of the consolidated or second mortgage bonds of the Power Company delivered to the Bates & Rogers Company by the Power Company in the settlement, the precise commitment of the Railway Company being to purchase such bonds, at the option of the Bates & Rogers Company, at eighty at the end of eighteen months. As a condition of this agreement the Railway Company demanded and procured the right to an additional exchange of five

hundred of its consolidated bonds then held by it for a like amount of first mortgage bonds. The precise agreement between the Power and the Railway Company is set forth at pages 418 to 421 of the Record.

What was done after the execution of this agreement is shown in the testimony of Mr. Hendee (Record p. 259) as follows:

> "In connection with the contract mentioned in the minutes of December 27, 1912, with respect to the settlement of the Bates & Rogers controversy, the Railway Company delivered to the Bates & Rogers Company one hundred shares of the common stock and fifty shares of the preferred stock of the Railway Company, and twenty-five thousand consolidated six per cent bonds of the Power Company, with the requisition that the Railway Company purchase such bonds under the conditions and at the figures specified in the contract (80 per cent of their par value). Under these two agreements of September and December referred to in the minutes of those dates the following exchanges of bonds were made: January 3, 1913, $38,000.00; January 6, 1913, $492,000.00; January 13, 1913, $65,000.00; February 10, 1913, $123,000.00. The serial numbers of the Power Company refunding bonds (being the so-called first mortgage bonds secured by the mortgage which has been foreclosed) obtained by the Railway Company in these exchanges were as follows: Numbers 2501 to 2514; 2525 to 2534; 3051 to 3192; 3198 to

3213; 3219 to 3279; 3285 to 3754. (All numbers given are inclusive).

"None of the loans made by the Railway Company to the Power Company have been repaid by the latter. The Railway Company surrendered to the Power Company an equivalent amount of second mortgage or consolidated bonds for the first and refunding bonds taken by it as provided in such agreement.

"The total number of consolidated or second mortgage bonds issued by the Power Company was $1,800,000, of which the Railway Company now owns $854,000, and holds as collateral against loans $750,000. Bates & Rogers Construction Company holds $30,000, and the balance outstanding in the hands of the public is $166,000."

The testimony with respect to this meeting of December 27th is quite remarkable in that two of the witnesses, the Messrs. William and Sinclair Mainland, who were members of the Committee, disclaim emphatically any knowledge of the agreement having been made, and claimed no precise recollection as to the holding of the meeting at that time. (William Mainland, pages 314, 315; Sinclair Mainland, page 320). However, this would not seem as of importance as Mr. William Mainland admittedly conducted and closed the negotiations with Messrs. Bates & Rogers (pages 312-315, page 318), and signed, on behalf of both companies, the contract in question. (Page

421). The reasons for the Bates & Rogers transaction, from the standpoint of the Power Company, appear principally in the testimony of the managing director, Mr. Watson. (Pages 265-272, 279-280). It appears that these negotiations had been under way for about a year. They were formally considered at a meeting of the Executive Committee on July 24, 1912, which appears on pages 268-271 of the Record, and was strongly recommended by the Company's consulting engineer by a letter recited on page 280 of the Record.

The foregoing presents substantially the admitted facts in the case, and the only facts in the view we take of it that are material for a determination thereof. Points of conflict have been mentioned, and should analysis of any of the conflicting testimony or the inferences drawn therefrom become necessary during the argument it will be referred to in the brief.

The Court in its decision, after stating briefly the formal proceedings, said (pp. 133-134):

> "It thus appears that while in form the Priest committee has taken the initiative, the proceeding is in anticipation of the foreclosure sale and the distribution of the proceeds thereof; and, considering the substance only, the controversy is to be deemed to be one arising after the sale, with the Railway Company seeking an order distributing to it its proportionate share of the proceeds of the property, and the Priest committee, as bondholders, resisting, upon the grounds set forth in their

complaints in intervention. It is upon the assumption that such is the real nature of the proceedings that, for the convenience of the parties, and in deference to their desire, the issue is determined at the present time."

The Court then proceeded to sustain the validity of the certification of the 107 bonds (p. 134), and as to the 718 bonds held both the September and December transactions fraudulent as against interveners (pp. 135-151), but concluded by holding (pp. 151-152) that the Railway Company "should be recognized as having an equity in the bonds corresponding to the consideration it has paid out, of which the Power Company has received the benefit," and ordered an accounting for the purpose of determining the extent of this equity. On September 18th the Court rendered its Supplemental Decision (pp. 153, 154) as follows:

"The parties have now appeared by their respective counsel, and have agreed that the existing record touching the transaction of September 25th, 1912, should be construed as showing that the Railway Company advanced $250,000.00, and no more, for which it is entitled to credit under the principle of adjustment explained in the opinion filed August 24, 1914. From this amount, therefore, will be deducted the $140,000.00 due under the original contract, and the Railway Company will be decreed an equitable lien upon the 440 first mortgage bonds for the balance of $110,000.00, with interest, and

it will also be decreed the right to receive the 175 second mortgage bonds contracted for.

"As to the Bates & Rogers transaction, no additional evidence has been offered, and it is not thought that the Record shows that the Railway Company has parted with anything of value on account thereof or has any substantial equities in the premises."

Upon this decision decree was entered accordingly.

The Decree of the Court, in so far as material, is set forth in paragraphs III, IV, V and VI, on pages 157 to 162, inclusive, of the Record. Particular attention is here called to paragraph III and part of Paragraph IV, reading as follows:

III.

"That the alleged agreement of September 25th, 1912, which includes the proposed exchange of bonds of the issue secured by the mortgage to the plaintiff to the number of 500, having a par value of $500,000.00, for other junior or second mortgage bonds, having a par value of $500,000.00, entitled 'Consolidated First and Refunding Mortgage Bonds,' secured by mortgage to the defendants Bankers Trust Company and F. N. B. Close, and the exchange of such bonds made in pursuance thereof, are illegal and void, and that the said respondent Idaho Railway, Light & Power Company is not entitled to share in the proceeds of the mortgage sale of the property

covered by the said mortgage to the plaintiff, as the owner of said bonds, exchanged in pursuance thereof, and secured by said mortgage to the plaintiff, except as hereinafter provided."

IV.

* * * * *

"IT IS ORDERED, ADJUDGED and DECREED that the said Idaho-Oregon Light & Power Company, by its Receiver W. J. Ferris, is entitled to receive back from said Idaho Railway, Light & Power Company the 440 first mortgage bonds, secured by the trust deed to the plaintiff herein, which were exchanged as part of said transaction; that the said Idaho Railway, Light & Power Company, by its Receiver O. G. F. Markhus, is entitled to receive back from the said Idaho-Oregon Light & Power Company second mortgage or consolidated bonds to the amount of $440,000.00 which it, the said Idaho Railway, Light & Power Company, gave in said exchange; that said Idaho Railway, Light & Power Company by its Receiver is entitled to recover from said Idaho-Oregon Light & Power Company the sum of $110,000.00, being the amount advanced or loaned by said Railway Company to said Power Company in excess of the $140,000.00 which the said Power Company was entitled to receive, with interest at the rate of six per cent. (6%) per annum thereon, from the dates when the sums constituting the said $110,000.00 were so ad-

vanced, and that such advances and the dates thereof are as follows:

December 14, 1912, ...$40,000.00
December 16, 1912, ...$40,000.00
January 4, 1913, ...$30,000.00

that the said Idaho Railway, Light & Power Company, by its Receiver, is entitled to the possession, as collateral security for the repayment of the said $110,000.00 and interest, of the $440,000.00 of first mortgage bonds originally deposited by said Idaho-Oregon Light & Power Company as collateral for the loan agreed to be made on September 25th, 1912; it appearing that the $440,000.00 of first mortgage bonds are now in the possession of the said Idaho Railway, Light & Power Company, or its Receiver. IT IS ORDERED AND ADJUDGED that he retain the same, but not as the property of the said Idaho Railway, Light & Power Company but as collateral to the said indebtedness of $110,000.00 and interest, as above set forth, and that all second mortgage or consolidated bonds held by said Idaho Railway Light & Power Company, or its Receiver, as collateral to the indebtedness, or alleged indebtedness, growing out of the agreement of September 25th, 1912, be surrendered by said Idaho Railway, Light & Power Company and its Receiver to said W. J. Ferris, Receiver of said Idaho-Oregon Light & Power Company.

The latter half of Paragraph VI, which recites the

Bates & Rogers transaction, referred to in the answer is as follows:

> "IT IS FURTHER ORDERED, ADJUDGED and DECREED, that the said agreement for such further exchange is illegal and void, and the exchange made thereunder invalid and fraudulent, and that said Idaho Railway, Light & Power Company, or its Receiver, shall return to said Idaho-Oregon Light & Power Company or its Receiver the said 278 first mortgage bonds, having a par value of $278,000.00, and that the said Idaho-Oregon Light & Power Company or its Receiver shall return to said Idaho Railway, Light & Power Company or its Receiver the said second or consolidated bonds to the par value of $278,000.00, so far as they may be in its or his possession either now or in pursuance of the foregoing portion of this Order, and that so far as they may be already in the possession of the Railway Company the said Idaho-Oregon Light & Power Company and its Receiver shall relinquish all right and title thereto."

Paragraph VII decrees to the Railway Company the right to receive from the Power Company, second or consolidated bonds secured by mortgage to Bankers Trust Company, in the amount of $175,000, being the amount of bonds which the Bankers were still entitled to receive under the original contract of September 1911, under which they went into the enterprise. Paragraph VIII (pp. 163, 164) may be deemed material and is therefore quoted as follows:

"This decree is entered in advance of sale and distribution under the said foreclosure at the request of and for the convenience of the parties, and upon the agreement in open court, all parties hereto consenting, that this decree shall be regarded so far as such fact may be at any time material, as having been made after sale and upon distribution, and as upon an application of said Railway Company as bondholders to share in such distribution and as against objection by these intervening bondholders and that no objection shall be made to said decree by any party affected thereby at any time or place, upon the ground that the same is premature or untimely."

In addition to the evidence hereinbefore abstracted, the following occurred at the trial:

The Court admitted over the objection of the appellant, Railway Company, evidence consisting of financial reports of operations of the Railway Company showing its gross earnings, operating expenses, net earnings, fixed charges, etc., ostensibly for the purpose of "showing the condition of the Railway Company in 1912, as establishing a motive for the transaction in issue." Several of these offers were made during the course of the trial and the objections overruled and the testimony admitted. Similarly reports of the condition of the Idaho-Oregon Company both for a series of years and for the specific year 1912, were admitted over like objection. These offers and objections, the

rulings thereon and the substance of the testimony admitted, together with reference to the page of the record at which the objections and testimony appears, are shown at length in the Specification of Errors and will not be set forth here. For some purpose which is not disclosed, but which may be assumed to have been to show the prosperous condition of the Power Company prior to the Railway management, an audit of the Company was offered in evidence and admitted over a like objection on the ground of irrelevancy and immateriality, and will likewise be specifically referred to in the Assignments of Error.

This statement we believe presents as succinctly as can completely be done the questions involved in this case, and which will be hereinafter discussed.

SPECIFICATIONS OF ERRORS.

The errors specified, in the language of the Assignment of Errors so far as they are urged here, with references, where necessary, to the pages of the record upon which the matters assigned as erroneous appear, are as follows:

The said Decree is erroneous and unjust to the said defendants (appellants here) and to each of them, in the following particulars:

I.

Because the said Court erred in sustaining said Bill in Intervention and entering Decree thereon.

II.

Because the said Court erred in holding and decreeing that the agreement of September 25, 1912, for exchange of bonds of the issue secured by the mortgage to the plaintiff having a par value of $500,000, for junior or consolidated First and Refunding bonds secured by mortgage to the defendants, Bankers Trust Company and F. N. B. Close, having a like par value of $500,000, and the exchange of such bonds made in pursuance thereof to be illegal and void, and in holding and decreeing that respondent, Idaho Railway, Light & Power Company is not entitled to share in the proceeds of the mortgage sale of the property covered by the mortgage to the plaintiff as the owner of said bonds, except as thereafter provided in said decree.

III.

Because the said Court erred in holding and decreeing that at the time of said agreement of September 25, 1912, by which the said Idaho Railway, Light & Power Company was to loan $250,000, to said Idaho-Oregon Light & Power Company that the latter company was entitled at that time to receive upon demand $140,000 in payment for second or consolidated bonds to the par value of $175,000.00.

IV.

Because the said Court erred in holding and decreeing that all said transactions, to-wit, agreement for and making said loan the release of the Idaho-Oregon Light & Power Company of its rights to de-

mand and receive $140,000, in payment for $175,000, par value of consolidated bonds, the agreement for exchange of bonds by which the said Idaho-Oregon Light & Power Company surrendered first mortgage bonds and received back second or consolidated bonds and the several deposits and exchanges of the collateral in connection therewith were connected and inter-dependent and all constituted a consideration for the other.

V.

Because the said Court erred in holding and decreeing that said Idaho-Oregon Light & Power Company by its Receiver, W. J. Ferris, is entitled to receive back from said Idaho Railway, Light & Power Company the 440 First Mortgage Bonds secured by trust deed to the plaintiff and exchanged as part of said transaction.

VI.

Because said Court erred in holding and decreeing that said Idaho Railway, Light & Power Company, by its Receiver, O. G. F. Markhus, is entitled to receive back from said Idaho-Oregon Light & Power Company second mortgage or consolidated bonds to the amount of $440,000, which said Idaho Railway, Light & Power Company gave in said exchange.

X.

Because the said Court erred in holding and decreeing that the said Receiver holds said bonds not

as property of said Idaho Railway, Light & Power Company, but as collateral to an indebtedness of $110,000, and interest.

XIII.

Because the said Court erred in refusing to hold and decree that the said Idaho Railway, Light & Power Company, or its Receiver by virtue of said agreement of September 25, 1912, and the exchange of bonds made thereunder, was the absolute owner of $500,000 face and par value of said so-called first mortgage bonds secured by mortgage to the plaintiff, State Bank of Chicago, and entitled to share in the distribution of the proceeds of foreclosure sale on that basis.

XIV.

Because the said Court erred in refusing to hold and decree that the said Idaho Railway, Light & Power Company, or its Receiver, was the owner of $440,000 face value of said so-called first mortgage bonds secured by the mortgage to the plaintiff, and entitled to share in the distribution of the proceeds of foreclosure sale on that basis.

XV.

Because the said Court erred in refusing to hold and decree that the said agreement of September 25, 1912, and all transactions had thereunder were valid and enforcible.

XVI.

Because the said Court erred, on decreeing that

said contract of September 25, 1912, was invalid in refusing to hold and decree that the said Idaho Railway, Light & Power Company or its Receiver were nevertheless entitled to hold all bonds secured by it under said transaction, and to share in the distribution of the proceeds thereof up to the amount advanced by said Idaho Railway, Light & Power Company under the said contract of September 25, 1912, to-wit, $250,000, with interest at the rate of six per cent per annum from the dates of the various advances thereof as shown by the evidence, to-wit, on $100,000 from October 4, 1912, on $20,000 from October 31, 1912, on $60,000 from December 11, 1912, on $40,000 from December 6, 1912, on $30,000 from January 3, 1913.

XVII.

Because the Court erred in holding and decreeing that the agreement for further exchange of bonds made in December, 1912, under which bonds of the par value of $278,000, secured by the mortgage to the plaintiff, were procured by surrender of the so-called second mortgage or consolidated bonds secured by the mortgage to the Bankers Trust Company and F. N. B. Close, and under which agreement bonds of the par value of $278,000 were exchanged, was illegal and void, and the exchange of said bonds invalid and fraudulent, and erred in holding and decreeing that said Idaho Railway, Light & Power Company, or its Receiver, should return to Idaho-Oregon Light & Power Company, or its Receiver, the said first mortgage bonds of the par value of $278,000.00.

XVIII.

Because the Court erred in holding and decreeing that the Idaho Railway, Light & Power Company is entitled to receive from Idaho-Oregon Light & Power Company second or consolidated mortgage bonds secured by the mortgage to the Bankers Trust Company and F. N. B. Close to the par value of $175,000 on account of $140,000 charged against advances to the Idaho-Oregon Company, and erred in holding and decreeing that upon sale under foreclosure, said Idaho Railway, Light & Power Company should be entitled to share in the distribution of the surplus for second mortgage bondholders as holder of such bonds to the par value of $175,000 in addition to other second mortgage bonds held by it.

XIX.

Because the said Court erred in refusing to hold and decree that the said contract of December, 1912, for exchange of consolidated or second mortgage bonds for first mortgage bonds secured by the mortgage to the plaintiff was in all respects a valid and binding contract, and further erred in refusing to hold or decree that said exchange of bonds of the par value of $278,000 made under said contract was a legal and valid exchange and vested title in said 278 first mortgage bonds in said Idaho Railway, Light & Power Company, or its Receiver.

XX.

Because the said Court erred in refusing to hold and decree that the Idaho Railway, Light & Power

Company parted with valuable consideration in said exchange of 278 bonds last mentioned, and erred in refusing to decree it any reimbursement on account thereof upon ordering surrender of the so-called first mortgage bonds received under such exchange.

XXI.

That the Court erred in refusing to decree that the said Idaho Railway, Light & Power Company, or its Receiver, were the lawful owners and holders of said 718 bonds procured in said exchanges by virtue of said contracts hereinbefore mentioned in these assignments and in said decree, and entitled to share in the distribution as owners thereof.

XXII.

That the said Court erred in holding that said interveners, A. W. Priest, and others, as bondholders, were entitled to raise the question of the validity of the said contracts of September 25, 1912, and of the exchange of the bonds made thereunder.

XXIII.

That the said Court erred in admitting the following evidence over the objection of the respondents (appellants here) as herein noted. (Record pp. 203-206.)

MR. CUMMINS: The interveners now offer page two of the monthly report of operations of the Idaho Railway, Light & Power Company, for December, 1912, which was introduced as Exhibit 4, Fuller's Cross-Examination. It shows the gross earnings for

the month of December, 1912, and for the twelve months then ending also the operating expenses, the net from operation, taxes, net from operation and taxes, non-operating revenues, railway rental, amount available for fixed charges, the amount of interest, rental of joint facilities, total fixed charges, surplus, and construction account. It is offered for the purpose of showing the condition of the Railway Company in 1912, as establishing a motive, or tending to establish a motive, for the transaction which is in issue here. I might say in this connection that I expect to offer, for the same reasons, another sheet of the same report, and corresponding sheets of the same months of the Idaho-Oregon for the purpose of showing the conditions of these two companies at that time.

To which said offer said respondents, by their counsel, duly objected on the ground that the same was irrelevant, immaterial, not germane to the issues on trial, nor within the allegations which the respondents were by the order of the Court directed to answer, but involves matters entirely foreign thereto, and which respondents were expressly excused by the Court's order from answering, which said objection was by the court overruled, in the following language:

"This is somewhat remote but I think perhaps I shall let it go in, it may have some bearing upon the good faith and reasonableness of the transaction. The objections will be overruled."

To which said ruling respondents, by their coun-

sel, duly excepted, and still except, and which said exception was by the Court allowed.

Interveners Exhibit No. 5 was thereupon read in evidence, being said sheet showing the results of operation of the said respondent, Idaho Railway, Light & Power Company, for the month of December, 1912, showing for that month and for the twelve months of 1912 the earnings, operating expenses, taxes, non-operating revenue, railway rental and net earnings, of said respondent Idaho Railway, Light & Power Company, and the fixed charges against the operation of the same with interest during construction.

XXIV.

The said Court erred in permitting the following question over the objection of the said respondents, (appellants here) therein noted, to which answer was made as herein stated: (Record pp. 206-207.)

MR. CUMMINS: (Continuing reading Fuller Deposition). Q. This report shows earnings for twelve months of $165,471.71, and net from operations and taxes, $111,636.82; non-operating revenue $24,898.43; railway rental $89,604.49, making available for fixed charges $246,139.74. Will you state the character and from what source derived was the non-operating revenue of nearly $45,000?

To which question counsel for respondents objected on the ground that the same was irrelevant and immaterial and not germane to the issues on trial, nor within the allegations which the respondents

were directed to answer, which said objection was by the Court overruled, and to which said ruling the said respondents, by their counsel, duly excepted and now except, and which said exception was allowed.

A. "I presume this is the income from the Idaho-Oregon securities held by the Railway Company." Such second mortgage bonds as the Railway held at that time. This interest was paid in November, 1912, but not in May, 1913. The item $86,604.49, designated railway rental is the net earnings of the Railway Company, which at that time was only partially built, interurban street railway lines in course of construction; The gross earnings less operating expenses and taxes; that is the ordinary expenses of operation of the Traction property, the company being charged with current furnished by the Railway Company at a price of one and one-half cents per kilowatt hour.

XXV.

The Court erred in permitting the following evidence to be admitted pursuant to the offer and over the objection herein stated. (Record pp. 207-211.)

MR. CUMMINS: "I have heretofore offered sheet two of the monthly operating report of the Idaho Railway, Light & Power Company for December, 1912. I now desire to offer sheet eight of the same report, showing the liabilities of the Company. It is the balance sheet * * * as of December 31, 1912."

To which offer respondents, by their counsel, then and there objected, on the ground that the same is

irrelevant and immaterial, and not germane to the issues on trial, which said objection was by the Court overruled, and to which said ruling the respondents, by their counsel, duly excepted, and still except, and which exception was by the Court allowed.

Interveners Exhibit No. 27 was thereupon admitted, being condensed balance sheet of said respondent, Idaho Railway, Light & Power Company, as of December 31, 1912, showing the assets and liabilities of the Company as of November 30, 1912, and of December 31, 1912.

XXVI.

The Court erred in admitting the following evidence pursuant to the offer and over the objection herein stated. (Record pp. 212-214.)

MR. CUMMINS: "I also offer sheet two of the monthly operating report of September, 1912, of the Idaho Railway, Light & Power Company."

To which offer respondents, by their counsel, then and there duly objected, on the ground that the same was irrelevant, immaterial and not germane to the issues involved, which said objection was by the Court overruled, and to which ruling respondents, by their counsel then and there excepted, and still except, and which said exception was by the Court allowed.

Thereupon interveners Exhibit No. 28 was received in evidence, being a statement of results of operation of the respondent, Idaho Railway, Light & Power Company, for the month of September, 1912,

and for the nine months of said year 1912, ending with September 30, 1912, showing gross earnings, operating expenses, taxes, net earnings, non-operating revenue, railway rental and the amount available for fixed charges with said fixed charges, surplus and construction account with tabulated statement of interest bearing securities of said Company.

XXVII.

The Court erred in admitting the following evidence pursuant to offer and over the objection herein stated.

MR. CUMMINS: I offer sheet eight of the same report. (Record pp. 215-218.)

To which said offer counsel for respondents then and there duly objected on the ground that the same is irrelevant and immaterial and not germane to the issues involved, which said objections were by the Court overruled, to which ruling said respondents, by their counsel then and there duly excepted, and still except, and which said exception was by the Court allowed.

Thereupon interveners Exhibit No. 29 was read in evidence, being condensed general balance sheet of respondent, Idaho Railway, Light & Power Company, showing the property, plant, equipment, total assets and liabilities of the respondent, Idaho Railway, Light & Power Company, as of August 31st and of September 30, 1912.

XXVIII.

The Court erred in admitting the following evi-

dence pursuant to offer and over the objection herein stated. (Record pp. 219-229.)

MR. CUMMINS: I offer sheet two of the monthly operating report of the Idaho-Oregon Light & Power Company for the month of September, 1912; sheet eight of the same report; and sheet two and eight of the report of said Company for December, 1912.

To which said offer and to each part thereof, respondents, by their counsel, duly objected on the ground that the same was irrelevant, immaterial and not germane to the issues involved in the cause, which respondents were directed to answer, and which said objection was by the Court overruled, and the said sheets and each of them were admitted by the Court "for the purpose of showing the status of the business of the Idaho-Oregon Company as bearing upon the real value of the bonds," to which said ruling of the Court the said respondents, by their counsel, then and there duly excepted, and still except, and which said exception was by the Court allowed.

Said pages from said reports were thereupon introduced in evidence, being interveners Exhibit No. 30, results of operation of respondent, Idaho-Oregon Light & Power Company, for the month of September, 1912, and for the nine months of the year 1912, ending September 30th, 1912, both as compared with the year 1911, and showing gross earnings, operating expenses, net earnings, taxes and fixed charges and like data. Also interveners Exhibit No 31, being condensed balance sheet of respondent, Ida-

ho-Oregon Light & Power Company, showing its total assets and liabilities of August 31st and September 30th, 1912.

Also interveners Exhibit No. 32, showing results of operation for said respondent, Idaho-Oregon Light & Power Company, for December, 1912, as compared with December, 1911, and for the twelve months of 1912, as compared with the twelve months of 1911, including gross earnings, operating expenses, taxes and fixed charges of said report for said period.

Also interveners Exhibit No. 33, being condensed balance sheet of the respondent, Idaho-Oregon Light & Power Company showing the assets and liabilities of said Company as of November 30th and as of December 31, 1911.

XXIX.

The Court erred in admitting the following evidence pursuant to offer and over the objection herein stated. (Record pp. 230-231.)

MR. CUMMINS: I offer a sheet showing the gross earnings, the operating expenses, and net earnings of the Idaho-Oregon Company for each year from 1907 to 1912, inclusive, and ask that it be marked interveners Exhibit No. 40, re 718 bonds. These figures are derived from audits of the books of the Company, made by Marwick, Mitchell, Peat & Company, chartered accountants; first, an audit for the four years ending December 31, 1910, dated New York, May 8, 1911, addressed to William Mainland, Esq., President of the Idaho-Oregon Light & Power

Company. A part of the report reads as follows: "The balance sheet submitted, attached to our report of even date, in our opinion is a full and fair presentation of the financial position of the Company as of December 31, 1910, excluding any contingent liabilities or uncompleted contracts. * * * The operations of the company during the period of four years under review, after charging off all expenses applicable thereto, including maintenance and renewals, but before making provision in respect to depreciation of the physical properties, the amount of which, however, would be of relatively minor importance, during this period, resulted as follows:"

MR. MACLANE: The opinions of the accountants as to whether these are proper or otherwise, except as stated in the audit themselves, it would seem to me would hardly, * * * We don't want to permit the inference to be drawn that we are bound by the running commentaries of the auditors on their own audit.

MR. CUMMINS: Not at all. The audit for the year 1911 is addressed to the Board of Directors of the Idaho-Oregon Light & Power Company, and is dated May 8, 1912. The audit for the year 1912 is addressed to the Board of Directors of the Idaho-Oregon Light & Power Company, and is dated April 3, 1913. I understand that it is admitted, subject only to the general objection as to its materiality.

To which said offer respondents, by their counsel, then and there objected on the ground that the same was irrelevant and immaterial to the issues involved,

which said objection was by the Court overruled, and to which ruling respondents by their counsel excepted, and still except, and which said exception was by the Court allowed.

Thereupon the said Exhibit was introduced in evidence as interveners Exhibit No. 40, being as follows:

Year	Gross Earnings	Operating Expenses	Net Earnings
1907	189,045.89	98,586.48	90,459.41
1908	196,416.16	83,438.80	112,977.36
1909	215,579.57	73,531.31	142,048.26
1910	297,041.43	82,526.01	214,515.42
1911	361,297.47	128,399.62	232,897.85
1912	405,210.21	189,318.10	215,892.11

XXX.

The Court erred in admitting the fellowing evidence pursuant to offer and over the objection herein stated. (Record pp. 375-378.)

The following, being a request upon the Trustee to foreclose the mortgage to the plaintiff, State Bank of Chicago, was offered in evidence, to which offer the respondents, by their counsel, duly objected on the ground that the same was incompetent, irrelevant and immaterial, not germane to the issues on trial, and referred to matters transpiring long subsequent to any of such issues, which objection was by the Court overruled, and to which ruling the respondents by their counsel duly excepted, and which exception was by the Court allowed.

The instrument was thereupon received in evidence, being interveners Exhibit No. 39, a written notice by a committee of holders of bonds secured by the mortgage to the plaintiff of the default of the Idaho-Oregon Light & Power Company in failing to pay interest due April 1st, 1913, upon said bonds, and a request upon the Trustee to foreclose the said mortgage on account of said default.

WHEREFORE, the said respondents (appellants here) hereinabove named, pray that said decree be reversed and the District Court directed to dismiss the bill in intervention of the interveners, A. W. Priest, et al., and to render such decree as shall be meet and just.

BRIEF OF ARGUMENT.

POINTS.

The Specifications of Error may be grouped under the following points which will be used as main heads in the development of the argument.

I.

The interveners have no standing in Court to litigate the questions involved nor legal interest in their determination, because—

1. The contracts in question were voidable and not void.

2. The bondholders had received their consideration under the mortgage when the bonds were certified and cannot complain of their subsequent disposition.

3. The bill is essentially a stockholders or general creditors bill (their claims having been reduced to judgment) and cannot be maintained because:

(a) The interveners are neither stockholders or creditors.

(b) Assuming them to belong to the latter class, or to have rights equal with such creditors, there is nothing to show their status as creditors when the acts complained of were committed, and the record affirmatively shows that the creditors of that class were not prejudiced by the transaction.

These questions are primarily presented by Specifications or Error I and XXII, but are involved incidentally, in that the decree awarded the bondholders the relief which they sought, by Specifications of Error II, VI, X, XIII, XV, XIX, and XXI.

II.

Under the conditions prevailing, the transactions were not fraudulent nor subject to avoidance in the manner here attempted by stockholders or general creditors, nor was any person legally or morally injured thereby.

Under this point we consider particularly:

(1) The transaction of September 25th.

(2) The transaction of December 27th.

As to

(a) First mortgage bondholders.

(b) Second mortgage bondholders.

(c) General creditors.

(d) Stockholders.

(e) Receiver.

This point is raised by Specifications II, V, VI, X, XIII, XIV, XVII, XVIII, XIX and XXI, wherein the general validity of the questioned transactions is asserted.

III.

The transactions merely awarded the appellants, as holders of second mortgage bonds, reimbursement to the extent that they were entitled thereto by their expenditures contributing to the common security.

This proposition is in aid of the Specifications of Error involved under the preceding point, and is merely an affirmative argument in support of the proposition there asserted.

IV.

Assuming the invalidity of the transactions, the appellants should have been decreed to be the owners of the bonds to the full extent of the consideration they gave therefor, and should therefore have been awarded a lien against the entire 718 bonds, for

(1) The $250,000 cash advanced with interest.

(2) The value of the second mortgage bonds

(3) The extent of the commitment to Bates & Rogers.

(4) The value of the stock of the Railway Company.

This proposition is asserted by Specifications of Error III, IV, XVI, XX, and was recognized by the Court in its decision, but complaint is made of the limited extent of the reimbursement allowed .

V.

Evidence as to the financial history and situation of the Power and Railway Companies was not relevant to the issues and should have been excluded.

The specific complaints made are presented by Specifications of Error XXIII to XXX, inclusive. These will require but brief mention.

I.

The Interveners Have No Standing To Litigate The Questions Involved.

The question involved in this case is the validity of the disposal by the Power Company of bonds admittedly properly certified and delivered to the Company under the terms of the mortgage, to reimburse the Company for expenditures made by it from its earnings and the proceeds of the second mortgage bonds, and which might lawfully have been made in the first instance from the proceeds of the first mortgage bonds, as against the holders of other first mortgage bonds, for whose benefit such expenditures were made. Bonds thus obtained by the Company were exchanged for second mortgage bonds validly outstanding in the hands of the Railway Company, the proceeds of which in large measure had gone to make up the expenditures for which the Power Company was entitled to such reimbursement.

No question is made of over certification or fraudulent or illegal certification, but it is claimed in substance that the bonds so given in exchange are not entitled to participate in the proceeds of sale because the transactions were not formally authorized by the Board of Directors or Executive Committee of the Power Company; that if so authorized, such Board of Directors and Executive Committee consisted of the same persons comprising the like board and committee of the Railway Company, and that the transaction was a fraud upon the Power Company and its creditors including the pre-existing first mortgage bondholders. We proceed to a discussion of these questions.

1. *The Contracts Were At Most Voidable And Not Void.*

If the contracts be regarded as constructively fraudulent because of the identity of the agents of the two contracting parties, or actually fraudulent (and we cannot see how they can be regarded as actually fraudulent if the parties were acting at arms' length) they are voidable and not void. This being true they are good as against everybody but the contracting party prejudiced thereby, and if he is content therewith no third person can ignore the contract or set it aside.

The questions which the interveners seek to litigate here are, first, whether the contracts were properly authorized. That is, whether, as to the contract of September 25th, a majority of the quorum

of the Board of Directors voted for the contract, and, as to the transaction of December 27th, whether the Executive Committee, or any competent authority, ever even purported to authorize the same.

We pass the direct answers to these propositions, first, that the lower court did not determine this phase of the question, but assumed the contracts to be properly authorized; second, that the interveners failed to overcome the *prima facie* case made by the minutes and supporting testimony on these points; third, that the vital transaction of September 25th was admittedly authorized by unanimous vote; fourth, that the contracts were regularly and formally executed under the corporate seals of the companies and presumptively authorized; fifth, that whether formally authorized or not they were fully carried out and executed, and, assuming that the Company could have set the contracts aside while they remained executory, or within a reasonable time after they had been carried out, it could not now do so, and we ask by what right could the bondholders complain of the lack of authority of the corporate officers to make these contracts, assuming, now, that there is no other objection thereto. If the Company is satisfied and acquiesces in the situation and in the acts of its agents, the bondholders, so far as this feature of the case is concerned, have no right to interfere. Certainly excess of authority by an agent affords no ground of complaint to any other person than the principal.

The remaining ground upon which the contracts

are to be set aside upon the interveners' contention is that the companies had common Boards of Directors who could not, therefore, contract with themselves. This would only be true were the contracts for that reason void, and not merely voidable. Although the terms are loosely used in the books as interchangeable, yet there is a clear legal distinction, in that if the transactions were void they are as though they had never been. If merely voidable, they are binding until set aside by a party entitled to avoid them, in this case, the corporation. If the contracts are merely voidable, then the question here raised by the interveners is substantially the same as the question last above discussed.

Let us then consider whether contracts between companies having common Boards of Directors are void or merely voidable.

It is generally held, by the Federal Courts at least, and the most of the State Courts, that transactions between companies, having common Boards of Directors, are not thereby rendered void, nor are they even presumptively fraudulent, but such transactions are voidable, if in fact unfair, at the instance of the company defrauded, or its stockholders, but they are not void and until avoided by parties entitled to avoid the same they will be recognized. It is further held that such transactions, even if otherwise voidable, are subject to ratification and that the performance of such contracts by both parties, and acquiescence therein by them, constitutes a ratification and precludes their subsequent avoidance.

The case most frequently cited to this point as the ruling case is Oil Company v. Marbury, 91 U. S. 587; 23 L. Ed. 328.

In discussing the general principles covering contracts of this character, the Court said:

> "The first question which arises on this state of facts is whether defendant's purchase was absolutely void."
>
> "The general doctrine, however, in regard to contracts of this class, is, not that they are absolutely void, but that they are voidable at the election of the parties whose interest has been so represented by the party claiming under it. We say this is the general rule; for there may be cases where such contracts would be void *ab initio;* as when an agent to sell buys of himself, and by his power of attorney conveys to himself that which he was authorized to sell. *But even here, acts which amount to a ratification by the principal may validate the sale.*"
>
> * * * *
>
> "*If he should be a sole director*, or one of a smaller number vested with certain powers this obligation would be still stronger, and his acts subject to more severe scrutiny, and their validity determined by more rigid principles of morality, and freedom from motives of selfishness. All this falls far short, however, of holding that no such contract can be made which will be valid."
>
> * * * *

"In this class of cases the party is bound to act with reasonable diligence as soon as the fraud is discovered, or his right to rescind is gone. No delay, for the purpose of enabling the defrauded party to speculate upon the chances which the future may give him of deciding profitably to himself whether he will abide by his bargain or rescind it, is allowed in a court of equity."

More nearly in point—that is, on the interveners' theory that the transaction is fraudulent—is Thomas v. Brownsville R. Co., 109 U. S. 522, cited to another point *infra*. There it was held that bonds issued under a fraudulent construction contract to a company having the same directors as the Railway Company was not void but merely voidable at the election of the parties affected by the fraud, and could be ratified or avoided by them.

In Jesup v. Illinois Central R. Co., 43 Fed. 483, Mr. Justice Harlan, sitting in Circuit, said:

(Quoting from page 503.)

"The fundamental error in the argument for the Dubuque Company is in the assumption that the lease was absolutely void by reason of Jessup and other directors, who were interested in the Cedar Falls Company, having participated in the making of it. We have already indicated that, so far as the lease depended upon the action of the board of directors, its technical validity was placed beyond question by the approval

of the majority of the directors, no one of whom then or ever had, so far as the record shows, any interest in the Cedar Falls Company. But to avoid misapprehension it is well to say that, in the judgment of the court, the lease would not have been void, even if a majority of the directors of the Dubuque Company occupied the same relations to the Cedar Falls Company that Jessup, James, Frost and Smith did when the lease was made. It would, at most, have been simply voidable at the election of the Dubuque Company, or, in a proper case, at the suit of its stockholders, and that election must have been exercised, or the suit brought, within such time as was reasonable, taking into consideration all the facts and circumstances of the case, including the nature of the property that was the subject of the lease."

In Robinson v. M'Cracken, 52 Fed., 726, it is said:

"But, assuming the existence of Mason's character as a stockholder, and that an exorbitant contract of the entire body of stockholders for their own pecuniary benefit can be seasonably attacked by existing creditors, it is well settled that, as a general rule, contracts of a corporation, which were made by directors who obtained a personal pecuniary benefit thereby, are not, on that account alone, void, but are voidable at the election of the parties who are affected by the fraud. This is clearly announced in Barnes

v. Brown, 80 N. Y. 527; Barr v. Railroad Co., 125 N. Y. 263; 26 N. E. Rep. 145; Oil Co. v. Marbury, 91 U. S. 587; and Thomas v. Railroad Co., 109 U. S. 522; 3 Sup. Ct. Rep. 315. In the latter case it is said, in substance, that those for whom the agent was acting have the option to avoid such a contract, but until they exercise their option, and seasonably show that it is their purpose not to submit to the act of the agent, the contract is in existence, and is not a nullity."

See also, *Coe v. East R. Co.*, 52 *Fed.* 531.

A strong case is that of Barr v. New York R. Co., 26 N. E. 145. The syllabus is as follows:

"1. In order to construct a connecting line for a railway company, a new company was organized, some of the directors and incorporators being directors of the old company. The new company made an agreement for the construction of its road, whereby it was to issue to the contractor $1,000,000 of 7 per cent bonds, and $500,000 of capital stock, being all the bonds and stock of the company. The contractor was a mere figurehead representing a syndicate of the directors and assigned both the securities and the contract to them. The actual cost of constructing the road was $850,000, and after completion it was leased to the old company which agreed to pay a rental equal to 30 per cent of the new road's gross earnings, and guaranteed that such sum should never be less than $105,000

per annum, or 7 per cent on the total issue of bonds and stock. Held, that, while the lease was made in pursuance of a corrupt scheme to impose upon the old company an obligation for the benefit of some of its own directors, yet it was merely voidable, and not void."

The Court, among other things, said:

"The question which is raised by the defense to the action is whether the fraudulent nature of the acts and proceedings, by which the railroad was constructed, and the contract of lease effected, are matters which have reached in their vice so far as, at this day, to disable the plaintiffs from enforcing against the lessee of their company the payment of the full amount of rental stipulated for in the lease. I cannot think that such is the result, or that the law intends such consequences to attach, as the respondent claims, and as the courts below have held. There is something repugnant to our sense of justice, and a seeming subversion of ideas respecting property rights, in the position that property may be retained and enjoyed, and payment of the stipulated rental therefor refused by its holder, on the plea of fraudulent practices, or because of the immoral conduct involved in the making of the contract by which the property was transferred, and the obligation to pay imposed. We would naturally reason that these considerations furnished grounds for repudiating a transaction so tainted, and for re-

fusing to remain under the obligation to keep and pay for the use of the property; but our reason fails to make it evident how, with knowledge of the fraud or immorality practiced, and with opportunity to act in repudiation, the party may retain possession and enjoy the advantages which possession gives, and, nevertheless, refuse the payment which was the condition of the right to its possession and use. Fraud furnishes ground for rescinding a contract, and for avoiding an obligation imposed, but I do not understand that, while serving to divest the obligation, it can be availed of as a means of continuing the possession of the property which the contract, legal in itself, was designed to and did transfer."

See also *Kelley v. Newburyport R. Co.*, 6 N. E. (Mass.) 745; *Nye v. Storer*, 46 N. E. (Mass.) 402.

See also *San Diego R. Co. v. Pacific Beach Co.*, 33 L. R. A. (Cal.) 788, and note.

A case somewhat in point on the general features of this case and in answer to contentions which are made on the argument is Leavenworth v. Chicago R. Co., 134 U. S. 688; 33 L. Ed. 1064.

There it was held that the fact that some of the trustees in a railroad mortgage were directors in another railroad company which procured the foreclosure of the mortgage, that one person was president of both companies, and a majority of the direc-

tors of both were the same persons, and a majority of the stock of the mortgagor was in the hands of the president of the other company, and that the attorneys were, or had been, attorneys for both companies, were not sufficient, in the absence of actual fraud, to render the foreclosure void. It was held in effect that it would have to be shown, to defeat the foreclosure, that the mortgagor company did not owe the interest or that the means were on hand to pay it, and the fact was suppressed or concealed by collusion between the companies.

On the question of ratification by the stockholders of a transaction voidable because of the existence of a common board of directors, see San Diego Co. v. Pacific Beach Co. *supra*, where the Court said:

> "The contract, therefore, was not void; and assuming that it was voidable, and might have been avoided by the appellant at the proper time and in the proper manner, it is clear that it was not so avoided, but that it was ratified. In the first place there was no attempt to avoid it, nor any intimation of such intention, until long after the time mentioned in the contract had expired, and respondent had performed all its covenants therein provided, until long after appellant had received all the benefits coming to it from respondent's performance, and until long after it had become impossible to restore anything to respondent, or to put it, in whole or in part, in *statu quo*. And during this time appellant without objection paid, from time to time, the greater

> part of the principal and a large part of the interest which by the contract it had promised to pay; thus inducing respondent to perform the whole of its part of the contract in confidence that appellant would do the same. This, we think, under the circumstances of this case, constitutes ratification by acquiescence; for the rule is that a party cannot repudiate the burdens of a contract while enjoying its benefits."

Whatever view the court may take as to the propriety of this inter-corporate action, in view of the relations of the directors to both companies, neither the corporation, nor its stockholders, are here seeking to avoid the transaction. The interveners, as bondholders, are attacking it as a fraud by the company upon their rights, and the company has been called upon to defend and is defending it. There is no privity of relationship between the bondholders and the company or its stockholders by which the former are entitled to make this attack.

This point is substantially decided in Mining Co. v. Coosa Furnace Co., 95 Ala. 614; 36 Am. St. Rep 251, where the Court said:

> "But the duty which disqualifies the directors from binding the corporation by a transaction in which they have an adverse interest, is one owing to the corporation which they represent, and to the stockholders thereof. A principal may consent to be bound by a contract made for him by an agent who, at the same time,

represented an interest adverse to that of the principal. A *cestui que* trust may elect to confirm a transaction which he could have repudiated on the ground that the trustee had an interest in the matter not consistent with his trust relation. In like manner, dealings between corporations, represented by the same persons as directors, may be accepted as binding by each corporation and the stockholders thereof. The general rule, is that such dealings are not absolutely void, but are voidable at the election of the respective corporations, or of the stockholders thereof. They become binding, if acquiesced in by the corporations and their stockholders.
* * * * *

"The directors of a corporation, in the transaction of its business and the disposition of its property, do not stand in any such relation to the general creditors of the corporation as they occupy to the corporation itself and to its stockholders. They are not the agents of such creditors, nor can they usually be regarded as trustees acting in their behalf. The creditors are not entitled to disaffirm a transfer of the property of the corporation, made by its directors or other agents, merely because the corporation itself or its stockholders could have done so. When a disposition of the property of a corporation is assailed by its creditors, they are not clothed with the right of the corporation or of its stockholders to set aside the transaction, re-

> gardless of its fairness or unfairness, on the ground that it was entered into by representatives of the corporation who had put themselves in a relation antagonistic to the interests of their principal. The right of the creditor to impeach the transaction depends upon its fraudulent character. The question in such case is, Was the transaction which is complained of entered into with the intent to hinder, delay or defraud creditors?"

A bondholder is in no better position than a creditor in this respect. By the bill in this case it is claimed in effect that the responsible officers of the Power Company, being interested in the Railway Company, perpetrated, for the interest of the latter, a fraud upon the former, but there is no trust relationship between those officers and the bondholders such as to entitle them to maintain their bill.

In Van Weel v. Winston, 115 U. S. 228; 29 L. Ed. 384, it was held that bondholders under a railroad mortgage could not maintain a bill against the President of the Company and the Railway Company on account of fraudulent conversion by the President of the proceeds of bonds. The Court said:

> "Other transactions are mentioned as fraudulent, such as that Mr. Winston converted some of the money arising from these bonds to private use, and not to the purpose of the Company. The answer to this is, that Mr. Winston came under no obligation to see to the application of

this money as the bondholders might think it ought to be applied. They had bought their bonds, paid their money, and received their security. The money so diverted was the money of the Southwestern Company and not their money.

"The wrong done by Winston in that matter, if wrong there was, was done to that company and not to the bondholders. They had provided their own means of insuring the building of this branch road, by disbursing the money through the Rock Island Company, and it was successful. The road was built. There was no privity between Mr. Winston and these bondholders as to his use of money which they had loaned to the Company, which was no longer their money. The error which pervades the bill throughout is to treat this corporation, to which the bondholders loaned their money, as if it had no existence, as if they had loaned it to Mr. Winston and held his personal obligation that it should all be honestly applied, and he be responsible for the repayment of the loan. If Mr. Winston cheated this company out of its money, the right to redress for that wrong is in the company or in its stockholders. As a creditor of the Company, Mr. Van Weel has no right to interfere in the matter until he had a judgment against the company, with an execution returned *nulla bona.* He has not in this suit shown any right to use the name of the Company or of its stockholders to obtain redress for a tort committed on them."

Substantially similar, but possibly a stronger case is that of the United States v. Union Pacific R. Company, 98 U. S. 569; 25 L. Ed. 143, where it was held that the United States, as a holder of the securities of the Union Pacific Railway Company, had no right to enforce rights of the corporation against its controlling stockholders and directors, who, it was alleged, had profited at the expense of the corporation by illegal acts. It was said that the right of such action was solely in the corporation, and that it could not be made to bring the same against its will by the United States as a bondholder, or by virtue of any other right which the Government had in the property, even though the corporation was so corruptly dominated by those guilty of illegal acts, that it would not seek the relief to which it was entitled.

The case is of peculiar interest in connection with the case of Wardell v. Union Pacific Railroad, 4 Dillon 339, affirmed 103 U. S. 651; 26 Law Ed. 509, as in the latter case the stockholders successfully maintained a bill to set aside the very transactions complained of by the United States as a bondholder in the former case.

The only responsive argument which can be made to this position is that because the Boards of Directors of the two companies were the same it was impossible for the Power Company to repudiate the transaction, and that since the Railway Company owned very nearly all the capital stock of the Power Company it was practically impossible that any

stockholder should act for that purpose in its behalf. Should this argument be advanced the obvious reply is that it proves too much, namely, that those directly concerned in the transaction were the only ones interested, and accordingly that, since it appealed to them as a wise and proper thing to do, no cause of complaint devolves upon any other person.

We are not here considering any question of actual fraud as against bondholders or creditors, but simply the question of constructive fraud inferred from the personal identity of the Boards of Directors of the two companies, and the fact that in the sequel at least the transaction was presumably profitable to the Railway Company.

2. *The bondholders have received the consideration for which they contracted and are in no position to complain.*

It has already been shown in the statement that the mortgage securing the bonds held by the plaintiffs, as well as by the respondents, was an open one authorizing the present issue of $500,000 of bonds and future issues under specified terms and conditions. Approximately $2,500,000 of these bonds were outstanding in the hands of interveners and other bondholders, at the time of the execution of the second mortgage. There were at that time certified and in the treasury of the Company, approximately $305,000 additional bonds under the plaintiff's mortgage, and there have since been certified the balance of the bonds, about $413,000, making

up the disputed issues in the hands of the respondents. (Statement, *ante* pp. 24-26).

The bonds issued under the mortgage each recited:

> "This bond is one of a series of seven thousand * * * amounting in the aggregate to $7,000,000, the payment of all which bonds, with interest as aforesaid, is equally and ratably, and without preference of one bond over another, secured by a trust deed or mortgage duly executed and delivered to the State Bank of Chicago." (Record, p. 384).

The mortgage provided that the conveyance of the property to the Trustee should be:

> "In trust, however, for the equal and proportionate benefit and security of all present and future holders of bonds and coupons to be issued under and secured by this indenture * * * without preference, priority or distinction as to lien or otherwise of any bond over any other bond by reason of priority in the issue or the negotiation thereof, so that each and every bond issued and to be issued as aforesaid, shall have the same right, lien and privilege under this indenture, and so that the principal and interest of every such bond shall, subject to the terms hereof, be equally and proportionately secured hereby as if all had been made, executed, delivered and negotiated simultaneously with the execution and delivery of this indenture; it being intended that the lien and security of this indenture shall take

effect from the day of the date hereof, without regard to the date of actual issue, sale or distribution of said bonds, and as though upon the day of such date all of said bonds had been actually issued, sold and delivered to, and were in the hands of, innocent holders for value." (Statement, *ante* pp. 22,23).

The bonds other than the original $500,000 immediately certified and delivered to the Company, were held by the Trustee to be certified upon certain terms and conditions, for (a) the retirement of prior lien bonds, (b) in purchase of other property, and (c) to reimburse the company for expenditures made by it in plant additions and construction. (Statement, *ante* p. 24). It is not disputed that the Company has made the expenditures for these purposes which were necessary to entitle it to draw down these disputed bonds, as well as all the other bonds held by the interveners and other bondholders, from the Trustee, nor that such bonds were validly held by the Company as ~~assets~~ requisite in its treasury for issue or sale at the best price obtainable for the corporate purposes of the Company. (Statement, *ante* pp. 25, 26).

Under these circumstances we contend that holders of other bonds are not entitled to question the use to which these bonds were put by the Company, nor the consideration received by the Company in their sale, since they (the bondholders) have received the consideration for which they contracted

when they took their bonds, in the enhancement in value or enlargement of the Company's plant. The consequent liability of their bonds to be cut down on distribution by *pro rating* with other bonds is one of the conditions with which their bonds were burdened when they took them. The pertinent clauses of the mortgage have been quoted or referred to, and it seems entirely clear that so far as the bondholder is concerned, if the Company received in betterments or additions the values required by the mortgage, it has fulfilled the contract which it made with its bondholders, and by which it became entitled as against them to the additional bonds, to use as it saw fit for any legitimate corporate purposes. The Company is the judge of such purposes, and of the values which it receives on issuing the bonds to purchasers.

To illustrate, if the Company had made these improvements or betterments from earnings, many of which it doubtless did make from such source, it had the right, on funding the expenditures thus made by taking down bonds for its reimbursement, to pay the proceeds of such bonds in dividends to its stockholders, or the proceeds of such bonds could have been used in paying operating expenses, funding floating debts, taking up junior securities, or any other corporate purpose. In fact all these uses are usual ones of ordinary occurrence.

So in this case these expenditures were ones in the first instance which could have been paid for in bonds of this series, and the bondholder is in no way damaged by paying for the expenditures, first out

of other funds, and then reimbursing the latter funds from the proceeds of these bonds. The bondholder is entitled to one accounting of the expenditures, for the purpose for which his bonds are issued; he is not entitled to two accountings; he is protected to the extent that there must be an equivalence between the expenditures on plant account made by the Company, and the bonds issued by it, so that the bonds shall be secured by property of equivalent value but to use a homely saying, he is not entitled to have his cake and eat it, too. He can prevent the issuance of, or repudiate, bonds to which the Company is not entitled, but he cannot, in the absence of appropriate covenants in the mortgage, follow the proceeds or direct the manner of use of the bonds to which it is entitled.

There seem to be very few authorities in point, the cases involving the validity of holdings of corporate bonds, generally fall within the following classes: 1. Bonds illegally issued, without, or in excess of statutory authority. 2. Bonds issued in violation of the provisions of the mortgage such as fraudulent certifications or over-issues. 3. Bonds issued at discount or with stock bonus. 4. Bonds issued or disposed of in violation of covenants limiting their issue or restricting the use of the proceeds. 5. The validity of, or amount at which, bonds may be proved against a defendant Company.

None of these cases are of value in this connection although some of them may be referred to under later headings of the brief. The only cases which

throw any light on the subject here involved, which we have been able to find are the following:

In Beech Creek Company v. Knickerbocker Trust Company, 111 N. Y. Supp. 1030, application was made by plaintiff for the certification of bonds reserved under its mortgage for the retirement of underlying bonds. It appeared that the Company had obtained twelve thousand of its underlying bonds from its general funds, and demanded reimbursement therefor from the Trustee. The Court said:

> "Nothing can be clearer therefore, than that the intention and agreement was that the reserved $252,000 of bonds were to be issued as fast as the bonds under the earlier mortgage were presented for cancellation, so that in the end there should be none of the latter bonds outstanding, but all of the bonds under the later mortgage should have been issued. How the Coal Company procured the bonds of the earlier issue which it presented for cancellation was no concern of the holders of bonds under the later mortgage, nor of the trustees under that mortgage. It was and is immaterial whether the Coal Company purchased the bonds by means of the sinking fund, or by the use of its surplus earnings, or by the sale of bonds to be issued under the later and larger mortgage. All that the holders of these latter bonds were concerned with was that there should not be outstanding at any time more than $3,000,000 of bonds, in-

cluding those issued under the earlier, as well as those issued under the later, mortgage."

A similar case is that of Twin State Gas Company v. Knickerbocker Trust Company, 120 N. Y. Supp. 764. This action was likewise brought to compel the trustee to certify refunding bonds to reimburse the Company for its expenses in retiring underlying bonds. The Court granted the relief, saying:

"The purpose of the mortgage to the defendant was not to reduce the indebtedness of the Twin State Gas & Electric Company, but to substitute a single indebtedness for all the different classes of indebtedness of the company; indeed, one of the purposes recited in the mortgage is "to fund the indebtedness" secured by the underlying mortgages. The word "funding" as thus used, has a well-defined and definite meaning, viz: "the process of collecting together a variety of outstanding debts" against a corporation, payable at short periods, and substituting therefor a single form of indebtedness "payable at periods comparatively remote." Ketchum v. City of Buffalo and Austin, 14 N. Y. 356; People v. Carpenter, 31 App. Div. 603, 52 N. Y. Supp. 781.

"It is no concern of the defendant, therefore, when the plaintiff presents underlying bonds in exchange for refunding bonds, whether the underlying bonds have been canceled or not, or how the plaintiff obtained possession of them. All it has to do is to see that the bonds presented are underlying bonds. All that the holders of the

bonds given by the mortgage to the defendant are interested in is that there shall not be outstanding at any time more than $1,500,000 of bonds, including those issued under this mortgage, as well as those issued under the prior mortgages."

A similar ruling was made in the case of Charleston Illuminating Company v. Knickerbocker Trust Company, 122 N. Y. Supp. 994.

A discussion of the right of the company to have authenticated and delivered to it bonds to reimburse it for construction expenditures appears in Pittsburg R. Company v. Central Trust Company, 141 N. Y. Supp. 66. There it was held that the Company was entitled to such reimbursement regardless of whether or not the work was done before or after the execution of the mortgage. The decision is of no particular importance as it is confined to construction of terms of the particular mortgage. It is cited simply as illustrative of the practice of corporations to reimburse themselves for capital expenditures against the mortgage bondholders.

The case most nearly in point is Atwood v. Shenandoah R. Co., 85 Va. 966-978.

In this case it appeared that a railroad company had executed a mortgage limiting the amount of bonds which might be issued thereunder to $15,000 a mile. It later appeared that the road could not be completed for this sum and certain extensions were deemed desirable to put it on an operating basis. Therefore, a general mortgage was created authorizing an issue of bonds up to $25,000 a mile,

subordinate to the former mortgage, but to strengthen the security of the second mortgage bonds, the company caused to be certified and delivered all the additional bonds which could be obtained under the first mortgage for the proposed construction on the basis of $15,000 per mile, and pledged such bonds as collateral security for its second mortgage bonds. In upholding this transaction and denying the first mortgage bondholders the right to attack the same, the Court said:

> "It is not perceived that the railroad company, in thus pledging these fifteen hundred and sixty first mortgage bonds as security for the benefit of the general mortgage bondholders, did any injustice to or violated any contract right of the first mortgage bondholders. Acting under its charter, which authorized the extension of the road, the railroad company executed the first mortgage of April 1, 1880, to secure its bonds to an extent not exceeding $15,000 per mile of road then or thereafter to be completed. The road has been extended and completed, and bonds at the rate of $15,000 per mile, and no more, have been issued under and in pursuance of the terms of the first mortgage, the $2,270,000 of bonds, held by the first mortgage bondholders, and the $1,560,000 of extension bonds issued thereunder and pledged for the security of the general mortgage bondholders, together make the aggregate of $3,830,000 at $15,000 per mile of the line of road actually constructed.

"The proceeds of the bonds held by the first mortgage bondholders were expended entirely on the construction of that part of the road north of Waynesboro, not a dollar thereof having been expended south of that point; while the extension south of Waynesboro was built exclusively with funds derived under the general mortgage. Yet the first mortgage bondholders claim a lien over the entire line of road prior and superior to that of the general mortgage bondholders. The claim is preposterous. It is true that the general mortgage was made expressly subject to the first mortgage, but, be it observed, it is subject not to the rights of the present first mortgage bondholders merely, but to all the rights secured by the first mortgage, prominent among which is the right to issue and use the additional bonds here in controversy.

"Both lots of bonds were issued in virtue of one and the same authority, under the same mortgage, about the same time, and for the same purpose. Hence the rights of the first mortgage bondholders, as respects the fifteen hundred and sixty extension bonds, are precisely the same as those of the general mortgage bondholders; the second stand together as first lienors.

"Though these fifteen hundred and sixty first mortgage bonds issued and deposited as collateral for the general mortgage bonds be held to be valid securities under the general mortgage, and they certainly are such, how does that fact im-

pair in any way the contract rights of the first mortgage bondholders? Both lots of bonds were issued under and in exact pursuance of the first mortgage, and if one fails, the other must necessarily fail also—if one is not entitled to the footing of first lien, the other can have no claim to such a position. Suppose the railroad company had issued those bonds and put them on the market for the purpose of securing funds with which to aid the construction of the extension of its road, and it undoubtedly had the right to do so, in what worse position would the first bondholders be placed than they are by the application of them as strengthening plaster—as a first lien backing and support to the general mortgage bonds? It is certain that they would be in the same relative position now held by them, and that is the position of their own choosing."

(Quoted from pages 986-7.)

The transaction was further attacked on the ground that the banking firm which took the general mortgage bonds were the financial agents of the Railway Company, and two members of the same were officers and directors of the Railway Company. The Court, commenting on this phase of the case, said, after stating that their actions would not violate any fiduciary relations:

"On the contrary, they simply lent their money to the Railroad Company upon the terms prescribed by it, as any stranger might do, and took the security for the payment thereof pledged un-

der the general mortgage, and against this there is no bar in either law or morals. It cannot be maintained that the rule in question, or any rule, forbids a dealing of this character—nor has any case gone to the unreasonable extent of so holding. See note to Fox v. Marretta, 1 Lea. Cas. Eq. p. 237; Twin Lick Oil Co. v. Marbury, 91 U. S. 587; Hotel Company v. Wade, 97 U. S. 75.

"In the last named case it was said: But where stockholders sanction a contract under which directors loan money to the corporation, and its bonds, secured by mortgage, are given, if the money is properly applied, the corporation is estopped from setting up that the bonds and mortgage are void by reason of the trust relations which directors sustained to it. Here the Railroad Company not only obtained the loan on the terms dictated by it, but received the cash and actually expended it in the construction of the extension of its road. Could there be any higher sanction than this? We think not. It would be an almost barbarous rule that would forbid a transaction of this character, and one that would at least hazard the undoing of all the common transactions of mankind.

"Even in the cases when the equitable principle in question is given its widest sweep, the general rule is that the contract may be avoided at the election of the stockholders, or *cestui que trust*, upon the terms of restoring what the trustee or agent has parted with in the transaction."

In Weed v. Gainesville R. Co., 119 Ga. 576, holders of $83,500.00 of bonds secured by a mortgage covering $245,000.00 of bonds attempted to attack on foreclosure the rights of the holders of the remaining $161,500.00 of bonds on the ground that the contract by which they were issued sold them at 90 and gave as a bonus therefor $130,000.00 of capital stock fully paid up, these bonds and this stock being issued for the purpose of completing the railroad, and it being claimed in addition to the manner of the issuance of the bonds that the completion of the road in the manner contemplated violated a state statute as to competing railroads. The Court said, page 590:

> "The construction of the Gainesville Railroad did not lessen or increase, but created competition where none previously existed. But if the geographical situation or character of business transacted had made the Georgia and the Gainesville competing roads, the state, the stockholders, or the parties alone could have attacked the contract of March 31, 1883, as being ultra vires, or in restraint of trade. Bondholders are not authorized to act as guardians for the public or the parties, in having such a contract set aside or declared to have been illegal; certainly not in a case where the bondholder prays that the subscriber to the stock under such contract be held liable for the unpaid subscription."

Keystone National Bank v. Palos Coal Company, 43 So. 570. Bill was brought by a bondholder for

the benefit of himself and all other bondholders, as well as for general creditors for the annulment of certain mortgage bonds held by certain of the defendants on the ground that they were illegally disposed of by the company. The Court said:

> "While the bill prays specifically for the 'annulment' of certain bonds held by the respondents, the relief sought in this respect is inappropriate to the facts stated in the bill. The bond issue was for corporate purposes and benefits, and was made under corporate authority, and it is not pretended, in so far as shown by the facts stated in the bill, that there was any illegality in the issue of the bonds. The facts stated tend to show, not an illegal issue, but rather an illegal disposition of the bonds after the same had been legally issued. If the bonds were 'hypothecated' without consideration, and in this manner parted with and disposed of, this would be a corporate wrong. The remedy in such a case, it would seem, would not be the 'annulment' of the bonds, but a restoration of the bonds to the rightful custodian, and the relief should be sought and had in the name of the corporation."

The bill was accordingly dismissed.

See also Van Weel v. Winston, *supra*.

It cannot be argued that the execution of the second mortgage, or the issue of bonds thereunder, prevented further issues under the first mortgage, or any way subordinated the subsequent issues under

that mortgage. It is probably enough, in this connection, to call attention to the language of the second mortgage which has already been quoted, by which it is expressly made subject to all bonds, "Now issued or hereafter to be issued," under the first mortgage. (Record, p. 201.) Under such conditions it has been uniformly held that further issues may be made under the first mortgage, and that the bonds so issued are of equal rank with the remaining first mortgage bonds, and are prior to all issues under the second mortgage, whether earlier or later in time.

The leading case on this point is Claflin v. South Carolina R. Company, 8 Fed. 118. The opinion is by Chief Justice Waite. There it was held that first mortgage bonds, whether unissued in the hands of the company at the time of the execution of the mortgage or afterwards acquired by it, could be issued and reissued after the execution of the second mortgage, so as to carry with them the lien of the first mortgage as against the second. The Court said among other things:

> "The mortgage is not to the unsecured bondholders, or floating-debt holders, or to trustees for their security. It was made to secure bonds, the proceeds of which were to be applied to extinguish the one class of debts and retire the other. The mode in which this was to be done is not provided for. All that is left to the discretion of the company or its officers. No creditor can demand the bonds upon such terms as

he may dictate. He must submit to what the Company requires, or get no advantage from what has been done. His specific rights under the mortgage all depend on the bargain he makes with the Company in that behalf. He may, if the Company consents, exchange his claim for bonds, dollar for dollar, or less, or more; but until some arrangement has been made by which a bond secured by the mortgage becomes in some way connected with the unsecured bonds he owns, or the part of the floating debt he holds, he remains just where he was before the mortgage was made."

It further appeared in the case that unsecured bonds were afterwards exchanged for secured ones under the mortgage, and in some cases notes were given to the unsecured bondholders, which were secured by collateral pledges of the second mortgage bonds. As to this the Court said:

"The old bonds have been retired by the use of the new. There was no actual exchange of bonds, but the new bonds were put in the way of being applied to pay for the old ones. All this, as it seems to me, is within the scope of the mortgage. It may not have been judicious management, but it was within the discretion of the company. The only contract with the individual bondholders is that the mortgage security shall not be diverted from its designated uses. That bonds sold under a pledge to secure an old debt

carry with them the mortgage, cannot, as I think, admit of a doubt."

With respect to the issuance of first mortgage bonds after the execution of the second mortgage, the Court said:

"The second mortgagees voluntarily permitted the first mortgage to stand as it was. In this the second mortgage bondholders are represented and bound by their trustees. Whatever the Company could do with the first bonds before, it might do after, so far as any express limitations in the second mortgage were concerned. The lien of the first to its full amount was recognized, and nothing was said or done showing directly any intention to limit the power of the Company under it. Suppose, instead of a mortgage to secure bonds, it had been, under full legislative authority to that purpose, to secure a certain amount and description of notes, like bank-notes, to be put in circulation as money. Would any one insist that, if a subsequent mortgage should be given on the same property, which was in terms subject to the lien of the first, the Company would in this way be prevented from keeping its old notes in circulation, and taking them in and paying them out as before? Clearly not, I think. And why? Because the nature of the paper secured was such as to preclude such an idea. The notes were put out for circulation. They were to be used as money. When in the possession of the company they were for the time

being inoperative, but as soon as they were out their attributes as notes secured by the mortgage were restored. Such would have been the evident intent of the parties, and such, I am sure, is the effect the courts would give to what had been done.

"Here the bonds put out, while not for circulation as money, were intended as articles of commerce, to be bought and sold in the market, and passed from hand to hand as current negotiable securities. They were to be used in trade. When in the hands of the company their lien under the mortgage was suspended; but the moment they were out in the usual course of business, it again took effect as of the time the mortgage was given. Any other rule than this would materially impair the marketable value of this class of instruments, and tend to defeat the very object of their execution. The whole issue of such bonds must be treated as of the date of the mortgage, without regard to the time they were actually put out, unless the contrary is clearly expressed."

It is clear from all the cases discussing this subject that for the bondholder to maintain such a bill as is here attempted the bonds must have been issued in violation of some covenant of the mortgage restricting the issue, or directing the application of the proceeds thereof. Such a case is McMurray v. Moran, 134 U. S. 150; 33 L. Ed. 814.

The famous Hocking Valley litigation, which fin-

ally terminated in the decision of the New York Court of Appeals in the case of Belden v. Burke, 42 N. E. 261, is likewise illustrative of this principle. There there was an express covenant as to the use to which the proceeds of the bonds were to be put. It was held that bondholders that did not know of or rely upon such covenant could not maintain an action for the diversion of the proceeds of the bonds, and to enforce the covenant by compelling reimbursement of the funds so diverted. It was clearly assumed throughout the whole case that were it not for such covenant the bondholders would have no standing, and the whole question was whether or not the plaintiff was entitled to enforce such covenant.

Pertinent to the questions discussed here the following quotations from the opinion are offered:

> "The general attitude of the plaintiff is that he, as the champion and representative of all the bondholders, in default of the trustee whose duty it was to act, has the right to reclaim the fund so improperly diverted, and compel the Railway Company to apply it to the purpose to which it was originally devoted. * * *
>
> "Assuming that proposition, there would still remain other questions, of the gravest nature, which would also have to be resolved in his favor. Perhaps the most important one is embraced in the contention of his counsel that upon the certification and delivery of the bonds by the trust company, the trustee, to the railroad company,

they were at once impressed with a trust, lien or equity in favor of the trustee, for the benefit of the future purchasers, and that a breach of such trust by the use of the bonds for other purposes subjected all the parties engaged in it—whether the Railway Company or the defendants, or all of them—to liability to restore the proceeds obtained in violation of the trust, for the benefit of the holders of the bonds. The defendant's answer to the position is that the bonds had no inception or validity as obligations of the railway company until sold; that until then they were not property which could be the subject of a trust, and that at no time did the trustee of the mortgage have any property right or interest in them, legal or equitable; that the Railway Company held them, with the absolute power of disposition, and when they were delivered to Burke in exchange for the stock he acquired the absolute title, free from any trust, lien or equity in favor of any one. The defendant's answer to the plaintiff's claim on the theory of breach of the covenant, as a contract, would seem to be conclusive; and that is that he never made the covenant, but that contract, whatever its effect, was the act of the Railway Company, and that even if it were true that he caused it to be violated, by means of his control of the corporation, it does not follow that he is liable upon it, or that the plaintiff is entitled to sue for its breach in a court of equity."

The necessity in such cases as the one at bar of establishing a contract trust between the bondholder and the corporation, and the violation of that trust by the latter toward the purchasers of the bonds is further illustrative in Banque v. Brown, 34 Fed. 162, where it appeared that the complainants purchased a part of an issue of railway bonds in reliance upon representations of a prospectus as to the uses to which the bonds were to be put, and they were diverted from such purposes and used, it was claimed, in fraud of the rights of the bondholders. It was held that the trustees for the disbursement of the moneys occupied no fiduciary relations to the bondholders and could not be charged with an accounting at the suit of the latter. The opinion is too long to quote here.

The same general subject is discussed from another standpoint in Dillon v. Barnard, 21 Wall 430; 22 L. Ed. 673, where it is held that a provision in the mortgage for the application of bonds to the payment of a contractor created no trust in his favor in the funds realized from the sale of bonds under the mortgage, and could not be enforced by him.

None of these cases are exactly analogous to the case at bar, but the principles underlying them are the same. The whole case is one of contract between the bondholder and the company. In the case at bar the company agreed with the trustee for the bondholders that it would take down no bonds except for specified purposes. In so far as those purposes were

prospective the bondholder would clearly have a right to see that the company did not use the bonds or their proceeds for purposes other than those for which it obtained them, but where the purposes had already been accomplished and the company took the bonds to reimburse it for its expenditures made in accomplishing such purposes, then no question of diversion in the future use of the bonds could properly arise, and all the trusts upon which the company's rights to the bonds depended as against the bondholders were completely satisfied and performed. As stated in many of the cases which we have cited the company then became the owner of the bonds, and the question of its use thereof is one which concerns only the company and its stockholders. The fundamental difficulty with the interveners' position here is that they are in effect asking the company for something which, as between the company and them, belongs to the former.

The Idaho-Oregon Company is made a defendant and its corporate actions are being attacked because of an alleged fraud perpetrated by it against the bondholders. It is not a case where that company or its stockholders are seeking relief against the Railway Company for any fraud or unfair dealing perpetrated by the latter Company upon the former. No such question is involved. The only question here is whether these bondholders can attack the Power Company's right to issue these bonds for any consideration which it deemed sufficient, it being admitted that the bonds had properly passed from the

hands of the trustee into the treasury of the Power Company. We submit that this cannot be done.

3. *The Bill Essentially a Stockholder's or Creditor's Bill and Not Maintainable by Interveners.*

A brief summary of the contents of the Bill has been given in the Statement (*ante* pp. 10-14). From this analysis, as well as from the reading of the Bill itself, as contained in the Record, it will be observed that it is essentially a stockholder's or General Creditor's Bill, charging the Company and its directors with fraud, and, in so far as it presented a litigable matter in the cause (at least according to the decision of the lower Court), it charged the Company, through its corrupt Board of Directors, with having disposed of assets of the Company in fraud of the Company's rights, and, through it, of the rights of its stockholders and creditors, and asked for the removal of the Power Company, through a Receiver, from the dominating influence of the Railway Company, and the general administration of its assets for the benefit of creditors and others entitled thereto.

The whole theory of the bill is antagonistic to and not in aid of the foreclosure of the mortgage. It is specifically prayed that the decree of foreclosure be vacated. It is alleged and repeated that the foreclosure was unnecessary, that there was no actual default and that the foreclosure scheme was a fraud upon the Company. The specific allegation as to the 718 bonds here in question charges that the transac-

tion was, "As to the interveners and the Power Company, wrongful and fraudulent," and states that the bonds should be "called in and cancelled." The original bill contained no prayer corresponding with this allegation, and such prayer was substituted as an afterthought by amendments, (Record, pp. 47-50), we assume for the purpose of giving the interveners standing in the foreclosure proceedings if the Court should sustain them.

Following the theory of the bill, the decree (*ante* pp. 45-48) likewise proceeds, in effect, upon the theory that the Power Company was a going concern or was at least in the possession of a Receiver who was administering its property generally, and collecting its assets for the benefit of its general creditors and others interested therein; that these bonds in question were assets of the Company and therefore should be delivered to the Receiver; that the transaction was a fraud upon the Company, should be set aside, the parties restored to *statu quo*, and the Railway Company be put in the position that it was in, or should have been in, had it not been for the wrongful transaction.

Notwithstanding the allegations and theory of the bill, and the adjudications of the Decree conformable thereto, the Court sought to escape the obvious conclusion that such a Bill could not be maintained by these bondholders, by treating the Bill as an objection to the Railway Company's participation in the proceeds of foreclosure upon distribution proceedings, (*ante* pp. 42, 44). To facilitate the disposal of

the case, the appellants agreed that decree might be entered at this time, as if entered upon the coming in of the proceeds of sale, and upon this objection then being made by these interveners to a distribution of the Railway Company (*ante* pp. 43, 44, 49).

We wish to emphasize that there is no criticism of, or objection to, the Court's assumption in this respect, in so far as it is regarded as furnishing the formal data which the Court regarded as necessary to a decision at this time, but the difficulty is that the Court in this decision has regarded as a formal or adjective question what is really a matter of substance. The theory of the Bill, and the real theory of the decree, is that the transactions, when had, were frauds upon the Company and its creditors. If they were such frauds, then the Company or its creditors may avoid them, and the Bill is properly framed to reach such a result, assuming it to be filed by the persons injured, or their proper representatives, but if they were not frauds upon such persons, or if the bill is not filed by the persons defrauded, then the whole theory of the Bill and the whole theory of the decree fails utterly, and the failure is not cured by the assumption, though joined in by all parties, that the substantial question involved is presented in a different manner, and at a different time than that in which it has been presented.

Let us assume, then, that the transactions were frauds upon the Company and, through it, upon its stockholders, and could therefore be set aside by them. We are met by the propositions:

(a) *The Interveners Are Neither Stockholders Nor General Creditors.*

This proposition, we think, requires no argument. The interveners are admittedly not stockholders. It is true that bondholders are creditors, but they are not general creditors but specific lien creditors, and by the terms of the contract giving them their lien it was subject to *pro-rating* with these bonds in whose ever hands they might be found. One *cestui que trust* can have no interest in who his co-beneficiaries shall be so long as they are within the terms of the trust. It must be admitted that these bonds or their proceeds could have been used in payment of claims of general creditors, retirement of second mortgage bonds, or even in the payment of dividends. In none of these ways would these interveners have received any benefit. The bill attacks the transactions, and the decree directs the return of the bonds, not because they were disposed of and the distributive share of the bondholders unlawfully cut down, but because they were disposed of improvidently, and in such form as to benefit indirectly the persons making such disposal, instead of for the benefit of the stockholders and the general creditors of the Company. Assume this to be true, then those stockholders and those general creditors are the persons to make complaint. If they are content, the bondholders have no right to make it for them.

(b) *As General Creditors the Interveners Have Not Brought Themselves Within the Rule, and the Record Affirmatively Shows They Were Not Prejudiced.*

The Rule referred to is that "subsequent creditors cannot avail themselves of a defense which the corporation has not made and which was available only to the corporation. If the corporation chooses to acquiesce, a creditor who became such afterwards will not be heard to impeach the transaction. This is well settled in respect to a fraud practiced upon a debtor. If the debtor waives the right to impeach the transaction or elects to abide by it a creditor subsequent to the fact will not be suffered to inquire into it or question it. Graham v. Railroad Co., 102 U. S. 148; Porter v. Steel Co., 120 U. S. 673. So, where a transaction is within the general scope of the powers of the Company, but is in violation of some limitation of law upon the exercise of the power, it cannot be challenged by those who subsequently become prejudiced."

Toledo, Etc. R. Co. v. Continental Trust Co., 95 Fed. 497, loc. cit. 528, 529.

This case is peculiarly in point, because the complaint there made was of the disposal by a Railroad Company to a director of bonds at less than par in violation of the Ohio statute under which the mortgage was made and the bonds issued. In addition to the foregoing quotation the following language of the opinion is also pertinent (page 525):

"But we also affirm the decree upon this point upon another ground; that is, that none of the appellants were entitled to challenge the validity of the mortgage bonds. The railroad company made no such issue. Its answer was a formal traverse of the formal averments of the bill, and made no question as to the validity of the bonds under Section 3313, Rev. St. Ohio, issued by it, and secured under the mortgage sought to be foreclosed. This defense has been made only under issues presented either by the answers or intervening petitions of general and unsecured subsequent creditors of the railroad company. May such creditors rely upon section 3313 as a defense against the enforcement of a mortgage and mortgage debt existing when they became creditors, and of which they had notice through registrations? Are bonds sold by an Ohio railroad company at less than par to a director so absolutely null and void that any subsequent creditor may interpose the defense and destroy the obligation, even in the hands of an innocent holder for value? Are they so absolutely void that neither the company nor its stockholders can waive the objection or validate them by subsequent ratification or long acquiescence? The construction contended for by counsel for appellants is that the bonds are void to all intents, and in the hands of every holder, and that the defense to them may be made by any creditor of the company."

The Court concludes (p. 529) "The corporation

having made no issue and having chosen to acquiesce in the purchase of bonds averred to have been sold to the directors, the defense is not available to subsequent creditors."

In this case there is no allegation or proof as to when the interveners acquired their bonds, and they do not, therefore, establish the first essential condition upon which creditors may impeach the transaction.

Moreover, and, we think, more important, the record affirmatively shows that general creditors could not have been injured by the transaction, because the bonds exchanged and surrendered by the Railway Company for the bonds here claimed were likewise prior to the claims of general creditors. This point, however, we develop more fully under a later head of the argument, and we will not dwell upon it here.

II.

The Transactions Were Not Fraudulent Nor Subject to Avoidance by Stockholders or General Creditors, Nor Was Any Person Injured Thereby.

The transactions of September 25th involving the loan of $250,000 and of December 27th with respect to the Bates & Rogers settlement, each stand on somewhat different grounds in fact, and the facts pertaining to each should be separately discussed, although essentially the legal effect of both may be very largely considered together.

(1) *The Transaction of September 25th.*

The facts in connection with this transaction are

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(1) *The Transaction of September 25th.*

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set forth at length in the statement (*ante* pp. 29-40). In essence they are very simple and may be briefly summarized. The Bankers, Kissell-Kinnicutt & Company, were under contract to buy $1,500,000 of the company's second mortgage bonds to yield $1,200,000. Under this contract they had already purchased $1,325,000 of these bonds, and were obligated to purchase but $175,000 more, which would have yielded the company $140,000. The company was in immediate need of $203,000 (Record pp. 426-429, Exhibit F). To this estimate of demands of the company's manager the managing director Mr. Watson added for the next three months approximately $50,000, making a total of $250,000 (*ante* p. 34). The Company was not even approximating in earnings the interest upon its second mortgage bonds, and default upon those bonds, if the earnings or any cash available should be relied upon to pay that interest, would fall inevitably on November 1st, less than forty days from the date of the meeting of September 25th. In addition to these facts the company was confronted by competition in the heart of its market (*ante* pp. 32-33). The competitor had already obtained its franchise, built its line to Boise City, and had completed its soliciting campaign, having signed up contracts, the number of which there was at that time no means of determining. It had also established a new rate some forty per cent lower than the existing rate of the Power Company.

Under these conditions the Power Company ap-

plied to the Railway Company or, if you please, to its own directors, to consider the matter in the most unfavorable aspect from the standpoint of the Railway Company, for a loan of the estimated requirements to keep it going for the next six months until some policy for the future might be determined. The Railway Company, or the directors, exacted as conditions of this loan: 1. A release of the obligation of the Bankers to satisfy the balance of their commitment; 2. First and Refunding bonds which were in the treasury available for the purpose or subject to certification, in the ratio of two to one for the loan of the needed $250,000; 3. The exchange of $500,000 six per cent consolidated or second mortgage bonds held by the Railway Company for a like amount of the refunding five per cent first mortgage bonds, so far as such bonds might be available for the purpose. There was no likelihood that the full amount would be available, and in fact less than half the amount has ever been available.

Upon this phase of the case the court said (Record pp. 139-140):

> "That under the circumstances such an agreement was thought by anyone to be in the interest of the Power Company is wholly incredible. I cannot believe that an independent board of directors would have given to it a moment's consideration. The Company needed money it is true, but if it was going on with the Ox Bow development the sum contracted for was wholly inadequate for any useful purpose, and if the

work at that point were not to be resumed, there was no urgent need for so large an amount. Those who participated in the transaction are unable to give any reasonable explanation of the purposes for which the $250,000.00 were to be used, and apparently there is none. The company had available on demand $140,000.00, due upon the Kissel-Kinnicutt contract, and surely both upon the market and in fact its first mortgage bonds were worth in excess of fifty cents on the dollar, the basis upon which they were to be hypothecated to procure the loan. Under the conditions created by the agreement the possibility that there ever would be a redemption was so remote as to be negligible. The transaction therefore practically amounted to a sale of between $200,000.00 and $500,000.00 face value of the first mortgage bonds for an equivalent amount of seconds, which it is apparent must have been wholly valueless if the firsts were worth less than their face, and the surrender, without any real consideration, of the obligation of the syndicate to take $175,000.00 face value of the seconds at 80. There is but one rational explanation of the agreement, and that is that the interests in control of the Railway Company, and, through it, of the Power Company, having concluded that the latter was hopelessly insolvent, and that a reorganization was inevitable and a receivership probable, resorted to this expedient for saving to themselves as much of the wreckage as possible."

We do not think these conclusions are justified by the admitted facts in the case or by any inference which can properly be drawn therefrom. The money required was absolutely essential to keep the company afloat at all. The financial condition, as shown by the evidence of the interveners, was such that it could not meet its obligations and survive the 1st of November. The statement submitted by Mr. Markhus, the company's manager (Record pp. 426-429), which (p. 425) was prepared by him about September 1, 1912, and thereupon forwarded to the managing director Mr. Watson, showed in detail the need for $203,000 for the period ending December 31, 1912. This statement is likewise referred to by Mr. Mainland, one of intervener's principal witnesses (*ante* p. 39), as having been so sent to Mr. Watson, and is nowhere disputed. It is true that neither Mr. Fuller, Mr. Watson, Mr. Wiggin nor Mr. Hendee could recall the details of these financial requirements at the time their depositions were taken. But how could those details be better or more conclusively proven than by the identification of the estimate thereof made by the company's manager at the time? To this estimate it is true that $50,000 was added, possibly arbitrarily, but, if so, it was not unreasonable to assume that a company requiring over $200,000 for four months would require under conditions becoming increasingly adverse within the next three months the added amount. With this admitted testimony in the record then why does the court state and base his decree in part at least, upon the proposition that the money was not needed?

This statement is followed by the one that the company had available on demand $140,000 due upon the Kissell-Kinnicutt contract. The statement is true in fact, whether true in law has never been presented for adjudication. If it is true, as the court likewise assumes in its decision, that the second mortgage bonds were valueless, there might be a serious question as to whether the Bankers were obligated to complete the purchase of securities demonstrated to be worthless. In any event, it is entirely possible, assuming the directors to have been entirely honorable men, that they would not have called for the balance of this commitment under these conditions when it could do the company no real good. Or, looked at in a more unfavorable light, the Bankers, dictated by their own interests, might have refused to perform their contract, hoping to escape the obligation imposed on one ground or another, rather than to deliberately give up $140,000 which would in any event be the utmost measure of their liability. A compromise of such litigation or of this situation as an entirety by substituting the first mortgage five per cent bonds for the second mortgage bonds to the extent of the commitment involved would not have been unreasonable or corrupt. We feel satisfied that no court would hold that an insolvent corporation is bound, because it has an outstanding contract to sell its securities, to increase its indebtedness by completing such sale. We think therefore, that the second statement of the court that the Company had this sum available on demand is true only conditionally and with qualification.

The court next states that upon the market, and in fact, the first mortgage bonds were worth in excess of fifty cents on the dollar. We think there is not a word of evidence in the record to justify this finding. It is true that pages of the record (roughly, pp. 323 to 373) are devoted to establishing this proposition. That the bonds could have been sold by Kissell-Kinnicutt & Company or any bond house through whom they would place them, we admit; but would this court, or the trial court, have sanctioned a sale under the circumstances then existing? We call particular attention to the cross-examination of the witness Mr. Ranstead on pages 327 to 331 of the Record, and the testimony of Mr. Reynolds on pages 341 and 342 thereof. Without quoting this testimony in detail it is apparent that all the bond sales had during the year 1912 were generally based upon the proposition that a strong financial syndicate had gotten behind the properties of the Power Company, and would take care of any situation which might arise, and buyers generally were not aware of the Company's actual condition (Record pp. 343, 345). It would have been a palpable and inexcusable fraud, legal and moral, upon the public, approaching if not equaling criminality, to have brought these bonds out on the credit of the syndicate without stating the actual conditions. If the conditions were truly stated, viz., That the Company could not earn the interest upon those bonds outstanding at its present rates, and that those rates on January 1st would have to be cut to meet compe-

tition at least forty per cent, in addition to the loss of all business which the competitor might get, we do not think the bonds were worth fifty cents on the dollar, or any other sum of money. They simply could not have been marketed.

Doubtless what the court means is that upon the distribution the bonds would have realized fifty cents. Whether that is true or not remains to be seen. There is nothing in the Record to show what they are worth further than the stipulation on page 381 that "The properties of the Power Company should be deemed of less value than the aggregate of the first mortgage bonds; that is, that they would not bring the amount of such bonds on foreclosure sale." There is nothing to show that they were worth twenty-five cents on the dollar, and we think we may state as a proposition judicially known, that dissenting bonds not included in a reorganization, on foreclosure of a corporate mortgage may not realize more than from ten to twenty-five cents on the dollar. If in fact the Railway Company had procured the entire 718 bonds as security for its loan of $250,000 and interest, there is nothing to show, and we do not believe that it will have more than enough—if enough—security for such loan.

Turning to an affirmative argument, we submit that the Record here shows that the Power Company, particularly its stockholders, received a very valuable consideration through this transaction, namely, the maintenance of the company as a going concern until such time as its future could be considered and

determined in the light of the new conditions which were to surround it. It could not pay the interest on its second mortgage bonds under the existing conditions. That had been demonstrated and consequently a reorganization was inevitable. But how extensive the reorganization must be, could only be determined after gauging the actual effects of competition, and with a view perhaps to the possibility of determining whether a reorganization could be effected with the co-operation of the competitor, embracing both companies in a consolidation. Competition in public utilities usually results in consolidation within a very short time. The economic, judicial and legislative history of this country conclusively demonstrates this fact. The public service commission laws of the last ten years recognize it in providing for regulated monopoly as distinguished from unregulated competition. That the Power Company, then, under these conditions, should be maintained for another six months was of great value to it.

We therefore submit that the transaction of September 25th was a fair and equitable one and beneficial to the Power Company, and that the identity of the two boards of directors resulted in no prejudice, or violation of trust owed to the Company.

(2) *The Transaction of December 27th.*

The facts in connection with this transaction have likewise been fully hereinbefore stated (*ante* pp. 40-43). It clearly appears therefrom that there had

been a dispute of several months standing with Bates & Rogers on which settlement was pending. The statement of the Company's engineer furnished the reason for the settlement, as shown on page 280 of the Record as follows:

> "Mr. Rogers of Bates & Rogers Construction Company has been here for the last two or three days discussing the Ox Bow contract. He was very anxious to do the work on the basis *of the unit prices in the contract*, which were evidently not intended for the kind of work which you are now proposing to do. If done on this basis I should say that the work would cost $100,000 more than it would if the Company did it directly."

It was therefore to the advantage of the Company to get rid of this contract. The intervener's principal witness, Mr. William Mainland, gave at some length a history of these negotiations (Record pp. 312-315). It appears therefrom that the Bates & Rogers Company agreed to accept in settlement of their claim, besides certain cash, fifty shares of the preferred stock and one hundred shares of common stock of the Railway Company, and $25,000 of consolidated bonds of the Power Company if they should be guaranteed by the Railway Company at 80 on eighteen months time (Record p. 419). Mr. Mainland thought that Mr. Rogers would have accepted something else, but, however that might be, this is the consideration that he agreed to accept. The

Power Company therefore applied to the Railway Company or, to its own directors, if you please, to agree to this settlement, and to issue the securities and the guaranty demanded by the Bates & Rogers Company. The Railway Company acquiesced but upon its own terms. We may admit that those terms were harsh, but we submit that no one at that time who knew the conditions would have loaned the Power Company anything except upon harsh terms, and that under the conditions prevailing harsh terms are not to be construed as fraudulent terms.

Possibly what the Railway Company actually got under the contract or was entitled to receive in addition to what it was already entitled to receive under the contract of September 25th, should be considered, rather than what it was nominally entitled to receive by the face of the contract. As a matter of fact the Railway Company was entitled under the contract of September 25th to receive $282,000 face value of bonds more than it has ever received under both contracts. It has actually gotten nothing under the Bates & Rogers contract which it was not theretofore entitled to. The number of bonds thereafter transferred, and for that reason assumed by the court to have been transferred under the latter contract, was $278,000.

The court in its decision, says (Record p. 144):

> "From the testimony and the surrounding circumstances, no doubt is left in my mind that the Power Company could have made settlement

directly with Bates & Rogers with its first mortgage bonds at a comparatively small discount, and that the devious course was adopted not upon their demand or for the interest of the Power Company, or because of any necessity therefor, but for the sole purpose of furnishing a pretext for getting the first mortgage bonds out of the treasury of the Power Company and into the hands of the Railway Company, and for the interest alone of those by whom the latter company was dominated."

The court further said (Record p. 143) that the Railway common stock was worthless, its preferred stock worthless, and its obligation to buy the bonds unenforcible "because of its insolvency if for no other reason."

It may be admitted that the stock of the Railway Company, by reason of the appointment of a receiver therefor, as stated in the record, and its confession of its insolvency in December, 1913, may and will prove to be worthless. It may be admitted likewise that its obligation to buy, or guaranty of, the Power Company's bonds is equally worthless, although the record here does not support that statement. Does it follow or is it inferable, that these securities were worthless in December, 1912? Assuming, however, that they were worthless, Bates & Rogers wanted them and were willing to take them and the Power Company was released from an onerous contract which would have entailed an excessive

cost of $100,000 as estimated by its engineer in the construction of its plant, and should not some consideration be given to the benefit which the Power Company and its stockholders obtained in the cancellation of this obligation?

True, if the Power Company was hopelessly insolvent as then seemed to be the case, its rights may not be of great importance if their protection is secured at the expense of creditors, but that the creditors were not injured we will endeavor soon to show, and in fact creditors and the estate generally, including any interest which the stockholders may have, would be enhanced by disposing of a claim of the magnitude of that of Bates & Rogers. So likewise a stockholder's or other heavy liability of individuals interested in the corporation, might be avoided by the settlement of the claim.

Surmise and conjecture such as Mr. Mainland indulges in, as to what Bates & Rogers would have accepted in settlement of this claim, we think entirely beside the point. It is evident that they all felt, as stated in the testimony of Mr. Mainland (Record p. 313) that the Railway Company "*was the Bankers' Company*" and its guaranty would be good. The most that Mr. Rogers ever said about taking first mortgage bonds was "He would consider seriously accepting the first and refunding bonds at the regular and sale price, but absolutely refused to take the consolidated bonds without a guaranty." (Record p. 314). We think therefore, under the

conditions prevailing, that the Bates & Rogers transaction cannot be condemned as a fraud.

Assuming, however, that these transactions were for the advantage of the Railway Company and of no more than negligible advantage to the Power Company and that they were, if not actually fraudulent, at least constructively so by reason of the position of the persons obtaining the advantage thereby, does that fact give any legal cause of complaint to any person interested in the Power Company, and was any such person legally damaged? The only possible classes of persons interested in the Company, and who could have been damaged by such transactions or entitled to avoid ~~it~~ them, were the first mortgage bondholders, second mortgage bondholders, general creditors, stockholders, or a receiver. We will consider these in their order.

(a) *First Mortgage Bondholders.*

Let us consider the transactions in their baldest aspect and, as the Bates & Rogers transaction was considered by the Court, as simply a device on the part of the Railway Company to procure first mortgage five per cent bonds in exchange for second mortgage six per cent bonds then held by the Railway Company. We submit on this assumption that no person interested in the Company could conceivably have been damaged by the transaction in any way, except the first mortgage bondholders, whose distributive share on the foreclosure of their mortgage

is thereby cut down. This was *damnum absque injuria.*

It has already been shown at length that these bonds were legally certified by the Trustee, and delivered to the Company; that the first mortgage had been fed by the expenditures upon which these bonds were certified, and the security thereof increased in cost and presumably in value in the ratio prescribed by the mortgage as condition of certifying the bonds, the aggregate being considerably in excess of the face of the bonds so certified. Liability then of the interveners' first mortgage bonds to be cut down by bonds subsequently issued was one of the express terms of their contract. How are they injured by the fact that in the distribution of these bonds one creditor has been preferred to another?

This wrong to the first mortgage bondholders, if wrong it was, was essentially a breach of trust relationship which is erroneously, we feel, inferred by the Court to exist between the directors and those bondholders. But certainly aside from the proposition which we have heretofore advanced (*ante* pp. 82-84) that there is no such trust relationship on the part of the directors to bondholders, we contend that a trust cannot be inferred in express violation of, or repugnance to, the terms of the instrument creating it.

In so far as any such trust relationship involves individual liability it is expressly waived by that clause of the mortgage, by which it is expressly agreed (Record p. 396) "That the past, present and

all future incorporators, officers, directors and stockholders of the Company, shall not be individually liable to any extent, or for any purpose with respect to such bonds or the coupons thereon, or any of them, or for any thing or act done or omitted, and any such liability by statute or otherwise, is expressly waived." Certainly if the transactions here involved were frauds upon the first mortgage bondholders they would afford a right of action for damages against the persons doing them. If such right is waived, and the bondholder agrees to look solely to the security which he gets for his money then no right of action could accrue to him under the circumstances.

But regardless of this clause, other provisions make all bonds certified under and secured by the Mortgage "equally and proportionately secured" thereby, as if executed and negotiated simultaneously with the execution of the mortgage, "it being intended that the lien and security of this indenture shall take effect from the day of the date hereof, without regard to the date of actual issue, sale or disposition of said bonds, and as though, upon the day of such date, all of such bonds had been actually issued, sold and delivered to, and were in the hands of, innocent purchasers for value" (Record p. 386). Thus it is intended by the mortgage that every bondholder shall be entitled to but that fractional part of the security, which his bond bears to the total number of bonds which may have been certified, and be entitled to issuance under the mortgage, and it

was to obviate just such conflicts, we take it, as have arisen here, that this provision was made.

Therefore, we submit that the liability of these bondholders, the interveners here, to have their security impaired by the issuance of other bonds of equal security against the same property was one of the conditions of their mortgage with which their bonds were burdened, and the diminution of their security in this manner is in no sense a legal wrong.

Before passing this question, which we have already discussed at too great length, considering the exhaustive argument heretofore made in support of practically the same proposition, permit us to urge that if this act was a legal wrong to these bondholders because it diminished their security, notwithstanding the provisions of the mortgage subjecting that security to such diminution, let us say so and place our decision upon that ground. We feel that the trial Court has become impressed with the view that this transaction was of such a nature that the Power Company should have resisted it, and would have done so, except for its domination by the Railway Company and that that Company should not be permitted to profit by its dominating position over the Power Company, and upon discovery of the fact that the bonds were obtained in an improper manner the Court on its own motion should refuse to countenance the transactions and enforce them. We feel that this attitude, in which naturally we cannot share, is the only way in which the conclusion can be arrived at, that these interveners can contest these

bonds. The fundamental difficulty with the attitude, outside of the legal objection to its failure to distinguish between the respective rights and remedies of the various parties is that it obscures the essential integrity of the transaction, otherwise demonstrated by the fact that no objection is made to it by any person entitled to object, because no such person was injured thereby.

(b) *Second Mortgage Bondholders.*

It is stipulated in the record that the properties will not sell for sufficient to pay the first mortgage indebtedness (page 381). This being true we cannot see how holders of second mortgage bonds were prejudiced by these transactions. We have already shown that as to them the first mortgage bonds were legally issued, the first mortgage being expressly left open for additional issues which should be superior to the second mortgage.

The second mortgage in this respect provided (Record pp. 200-201):

> "Section 1. Seven Million Dollars ($7,000,000.00), par value, of said $1,000 bonds shall be reserved to be issued and delivered for the purposes of refunding, redeeming, purchasing, taking up, retiring or paying at, before or after maturity any and all bonds now issued or hereafter to be issued by the Company under and pursuant to the terms of a certain Indenture dated April 1st, 1907, between the Company and the State Bank of Chicago, as Trustee, which last men-

tioned bonds are hereinafter called "Underlying bonds," and the indenture securing them the "Underlying mortgage," under which Indenture the issue of $7,000,000 of bonds was authorized, but only two million seven hundred and ninety-nine thousand dollars ($2,799,000.00) of bonds have heretofore been issued and are now outstanding."

It is interesting to observe in this connection that all the bonds certified under the first mortgage whether previously actually sold or not are recited as outstanding. The total amount of bonds theretofore sold to the public was $2,494,000 (Record pp. 378, 379). The mortgage recites the number outstanding as $2,799,000.00.

The Court in commenting on this phase of the case said (Record p. 140):

> "Putting aside for the moment all question of rights of these interveners, it is plain that there was a breach of trust on the part of the officers of the Power Company and a disregard of the rights of the holders of approximately $166,000, face value of consolidated bonds which had been put upon the market and were held by the general public who would therefore be prejudiced by the issue of first mortgage bonds in exchange for the Consolidated, or seconds."

This would be true should the property sell for a sum in excess of the face of the first mortgage bonds, but in view of the stipulation that it will not

sell for that amount, we cannot see that the second mortgage bondholders were in any way injured. If there be a trust relationship between the second mortgage bondholders by reason of their interest in the common security, and the property should sell for enough to realize some funds for these bondholders, it might be that independent second mortgage bondholders would be entitled to claim an interest in the proceeds of the first mortgage bonds after reimbursing the Railway Company, for their share of the amounts advanced by the Railway Company in securing such first mortgage bonds. However, this question is not before the Court in any way. The Railway Company was the owner of approximately nine-tenths of the second mortgage bonds. It evidently sustained such relations to the holders of the other bonds that they have not seen fit to question the transaction in any way. Should they be entitled to participate with the Railway Company in the proceeds of these bonds such participation may be decreed to them at the proper time.

(c) *General Creditors.*

General creditors are not injured by the exchange, because the second mortgage indebtedness was ahead of them equally with the first mortgage indebtedness. There is no trust relationship between a company and its creditors, in which the latter can insist upon the application of the proceeds of the bonds to their claims, even where the mortgage expressly provides that the bonds shall be used for that

purpose. The trust in such case is to the bondholders and not to the general creditors.

Dillon v. Barnard, supra.

We have been unable to find any case in which it has been contended that general creditors, without an express provision in the mortgage, have any right to the proceeds of the bonds as such. The Company could have kept these bonds in the treasury, and upon distribution, the general creditors would not have come in until after the second mortgage had been satisfied, and in such case such creditors would be equally postponed to the second mortgage bonds as to the first.

Claflin v. S. Car. R. Co., supra.
Mining Co. v. Coosa Furnace Co., supra.

This position seems self-evident. The Court below evidently awarded the interveners relief upon the theory that creditors are awarded relief against preferences of Directors to themselves; an application of the trust fund doctrine (Record pages 145-149). If these bonds constituted assets in the treasury available to satisfy the claims of the general creditors, then unquestionably such creditors are injured by the transaction, unless the rank of their judgment as against the general assets of the Company would be subordinate to that of the second mortgage bondholders. We have not found any case wherein this question has been determined. So far as the argument here is concerned the proposition may be conceded, because, if conceded, these bonds

would share equally with all other bonds in the distribution of the assets of the Power Company, and the question would arise upon distribution as to whether the Railway Company or its general creditors, if there be such other than the Railway Company, are entitled thereto. If on the other hand as first contended under this sub-division there is no equity in favor of general creditors in these bonds they are clearly not damaged by the transaction in question. The interveners here would resist vigorously any attempt by general creditors to reach these bonds or to share in them. It is not in the interests of the general creditors that this litigation is waged but in that of the first mortgage bondholders alone.

(*d*) *Stockholders.*

The company's stockholders are not injured, because the company owed the same amount of money before the exchange as afterwards, with the exception of such new money as the company obtained. the only difference being that the obligation was formerly evidenced by second mortgage bonds and afterwards by first mortgage bonds. In either event there was the same aggregate indebtedness out ahead of the stock, and upon distribution the stockholders would not receive a dollar more if this exchange had not been made, than if it had been made.

The Company was under no more obligation to prevent the foreclosure of the first mortgage than of the second, and the rights of the stockholders would have been equally foreclosed, and

their interest in the company wiped out, by foreclosure of the second mortgage as of the first.

(*e*) *A Receiver.*

A receiver of the Company can have no greater rights than those of the persons whom he represents. *High Receivers, Section* 204, 205. The question of the rights of action of a receiver to redress on behalf of the corporation or its creditors for frauds committed by the officers and directors of the Company, is exhaustively discussed in *Great Western Mining Co., v. Harris, (C. C. A. 2d Circuit)*, 128 *Fed.* 321. It is there shown that any right of action to attack fraudulent transactions including over-issues of stock to Directors, accrues not to the corporation itself, which is a party to the transaction, nor to creditors generally, some of whom were such before the transactions were complained of, but only to the particular creditors defrauded, and therefore that such suit could not be maintained by the Receiver suing on behalf of creditors generally, or of the corporation.

However, we have doubtless followed this branch of the argument too far already. This bill is not brought, nor on the assumption of the Court is any objection made to these transactions, by Second Mortgage Bondholdeds, general creditors, stockholders or the Company's receiver. The receiver is merely the Court's officer to carry out his decrees and administer the property in accordance with his orders. He

has no interest in the question of the priorities between the creditors in the distribution of the common fund. In no view on the state of the record here shown has any person been placed in a worse position by reason of these transactions, except the First Mortgage Bondholders and their position is made worse not by any acts of the Directors fraudulent as to them, but solely by the letter and spirit of their contract, which they are seeking to transcend.

III.

The Transactions Merely Awarded Appellants Equitable Reimbursement for Their Expenditures.

Looked at from the standpoint of the creditor, the Railway Company, assuming the insolvency of the Power Company and the imminence of its liquidation and disregarding every consideration for the transaction involved save and except the surrender of the second mortgage bonds, we can conceive of no fairer act by a board of independent directors than the transaction here questioned consummated. The Railway Company, or, more correctly, its assignors, the Bankers, had contributed $1,060,000 in cash into the treasury of the Power Company. There is no complaint or question made here that every dollar of this amount was not expended honestly and properly in additions to the plant of the Power Company and thus augmenting the security of the first mortgage bondholders, and in the proper maintenance of the company as a going concern. It is expressly

conceded that from the proceeds of these bonds and the earnings of the company there had been expended on the plant account of the Power Company approximately ten-ninths of the face value of these bonds, and that such expenditures had been made for purposes for which such bonds might lawfully have been issued in the first place. This is, of course, exclusive of all expenditures made from the proceeds of these second mortgage bonds on account of the Ox Bow development for which the first mortgage bonds could not have been issued. Under these circumstances we ask, why should the interveners be entitled to alone share in the proceeds of the first mortgage and to exclude therefrom others who had equally contributed to the common security.

In this situation, where do the abstract equities lie? Shall the interveners be permitted to say to the stockholders, "we appreciate that moneys which might have been utilized in paying dividends to you have served to add to our security, yet you have no interest in the bonds which we agreed should be issued against such expenditures;" and to the second mortgage bondholders: "We quite agree that your bonds are worthless and that the moneys obtained from the sale thereof have increased our security to the extent of $1,200,000, or thereabouts but, notwithstanding that fact, your contract does not provide that you shall be entitled to any interest in the first mortgage bonds which we agreed should be issued against the use of the moneys which you so

provided, and, accordingly, we propose to retain all of such security, and, although, in accordance with our agreement, bonds have been issued under our mortgage against the expenditures of your money, you cannot participate in the security." Such, in substance, is the position of these interveners.

If we are correct in the conclusion that, when the bonds were certified and delivered to the mortgagor, they became its absolute property, obviously abstract equity required that they should be utilized to restore to the stockholders the earnings which had been used in adding to the first mortgage security and to repay the loans made by the second mortgage bondholders which had provided the balance of the funds utilized to further increase the security of the first mortgage bonds.

Indeed, although we are frank to say we have not found any adjudicated case supporting the proposition, on principle, we go further and submit most earnestly that, should the transaction in question be avoided and the bonds in controversy be restored to the treasury of the Railway Company, a court of equity should, upon distribution of the proceeds of a sale of the property covered by the lien of the first mortgage, permit the said bonds to share in such distribution, ascertain the sums contributed to the security of the first mortgage, respectively, from the earnings and from the proceeds of the second mortgage bonds, if such ascertainment be possible, and apportion the distributive share of such bonds

in the proportions determined; or, if such proportions cannot be determined, that such distributive share should be devoted to such purposes as to the court shall seem most equitable. We assert this proposition, because, to our mind, it is highly inequitable that, merely because the second mortgage indenture fails to provide that all first mortgage bonds, issued against property purchased with or improvements and betterments made from the proceeds of the sale of the second mortgage bonds, shall be deposited as additional security under the second mortgage, the holders of the other first mortgage bonds can retain the benefits derived from the money of the second mortgagees, without the latter being subrogated to the rights of the mortgagor in the bonds obtained by it through such expenditures. Indeed, we see no reason whatsoever why the principle of subrogation should not apply.

It seems to us that it is not necessary to defend these transactions to go to the length that we have in this discussion. There seems to be an assumption throughout the interveners position here, that as against the company and in the eyes of the law the first mortgage money is entitled to be regarded as much more sacred than the second mortgage money. We think this assumption entirely unfounded. One dollar of this money is just as good and entitled to just as much protection as another dollar, except as the parties have been able to secure for themselves better legal security. The company owed the money

on its second mortgage bonds, just as much as on its first, and was equally bound to repay it and protect its security in every way. If the company could get the second mortgage bondholders participation in the first mortgage under the terms of the latter instrument, we can see no reason why the second mortgage bondholders should not demand that it should do so, and obtain a satisfaction of their demand if able. So if the Company could reduce its second mortgage indebtedness, by issuing additional bonds under the first mortgage there is no reason why it should not do so. The first mortgage bondholders are entitled simply to the security for which they contracted, and so far as that security gives them a better position than the second mortgage bondholders they are entitled to it. But if the latter are able to secure participation in the first mortgage under the circumstances, they are likewise entitled to do that, and the court should seek to protect them in their investment equally with the first mortgage bondholders.

We therefore submit on the various grounds stated, that the assignments of error affirming the validity of these transactions should be sustained, that the decree should be reversed in toto, and that decree should be ordered in favor of appellants confirming their full ownership and the validity of these questioned bonds.

IV.

Assuming the Invalidity of the Transactions the Bonds Were Enforcible to the Extent of the Consideration Given Therefor.

If the delivery of these bonds to the Railway Company be regarded as fraudulent as against the Power Company and through it, the interveners, and such fraud can be urged by the interveners to defeat the claim of the Railway Company to the ownership of these bonds in their entirety, the Railway Company would nevertheless be entitled to hold the bonds, and to receive dividends thereon, up to the amount of the value parted with by the Railway Company.

(a) *The Principle of Rescision.*

The Bill in Intervention, as has previously been shown, is in essence a stockholders or creditors bill to set aside the transaction, both for fraud and want of authority in the responsible officers of the corporation to enter into the same. In such cases the authorities are uniform that the transaction can be set aside only upon condition of return of all considerations received, and the restoration of *status quo.* This Court has further expressly held that unconditional offer to do equity in this respect must be made in the bill itself, and that even an offer to credit the amount on any judgment recovered against the defendant is insufficient.

Alaska & Chicago Commercial Co., v. Solner, 123 Fed., 855.

See also, for applications of the general principle,

New Castle R. Co., v. Simpson, 23 Fed. 214.
Fleckenstein v. Waters, 160 Mo., 649.
Barr v. New York R. Co., 125 N. Y. 263.
Jones v. Green, 129 Mich. 203.
Hitchcock v. Barrett, 20 Fed. 653.
Symmes v. Union Trust Co., 60 Fed. 830.

Other cases hereinbefore cited likewise establish this proposition, and the decree entered by the District Court here recognizes the principle, although, as we shall endeavor hereafter to show, does not fully enforce it.

(b) *Enforcement of Fraudulent Bonds.*

If we assume, as the trial Court assumes, that the proceeding in essence is a part of the foreclosure, and that the Railway Company is an actor seeking to procure its distributive share upon its bonds, the principle is not fundamentally different, although it may be expressed in a different way, and, as we have said above, the Railway Company, although it cannot enforce the bonds in their entirety because of the fraud, is nevertheless entitled to enforce them up to the amount of the value given by it therefor.

This question is authoritatively settled in Thomas v. Brownville, etc., R. Co., 109 U. S. 522; 27 L. Ed. 1018. There suit was brought to foreclose a mortgage under which bonds were issued on a construction contract, in which the directors of the corporation issuing the same were interested, and from which they received benefits clearly detri-

mental to the interests of the Railway Company. *Stockholders* intervened setting up the defense that the bonds were fraudulent, and asking that they be cancelled. On a reference to a master it was found that the construction company had actually expended about $200,000, in building the road under the fraudulent contract. The lower court, however, refused to allow recovery even of the amount actually expended. On appeal to the Supreme Court the latter said that the contract was not absolutely void, but voidable at the election of the parties affected by the fraud; that it could be ratified or avoided by them; that the bonds and mortgage to the extent of the consideration which the company received were good and enforcible.

The court further said:

"There is another principle of equity jurisprudence which leads to the same conclusion.

"The stockholders who have resisted complainant's claim were not parties to the original suit for foreclosure, nor were they either necessary or proper parties as the case then stood. The decree and sale were made in a suit where all the usual parties to such a suit were agreed.

"These stockholders had no legal right to interfere. It was only by permission of the court that they were allowed to come in and contest the validity of the mortgage. In doing this, they became actors. They filed their cross-bill.

"In this condition of the case they are amen-

able to the rule that they who seek equity must do equity. It is just that they should pay a fair price for what they have received; that this mortgage, given for the construction of the road, though excessive by reason of the fraud in the contract, should stand for the reasonable value of what the company actually received in the way of construction. To permit these interveners to defeat the mortgage on any other terms would be unjust and would make the court the instrument of this injustice.

"The decree of the Circuit Court, therefore, be reversed and the case remanded to that court, with directions for a decree in favor of the plaintiff for the sum of $205,947.66, with interest. If a sale becomes necessary, this sum must be paid out pro rata on the bonds secured by the mortgage, on their being produced and canceled, or surrendered for cancellation, provided the road sells for so much."

See also,

Wardell v. U. P. R. Co., 4 Dill 339; affirmed 103 U. S. 651, 26 L. Ed. 509.

Foster v. Mansfield R. Co., 36 Fed. 627.

Thomas v. Peoria R. Co., 36 Fed. 816.

It is unnecessary to pursue this question further, at least upon the principal appeal which is the subject of this brief, as the Court recognized it both in its decision (Record pp. 151, 162) and in its decree (*ante* p. 47). The complaint against the Court's de-

cision is that it limited the bonds against which the Railway Company was entitled to enforce its claim for advances made to those originally pledged technically as collateral security, viz: $440,000 (*ante* pp. 44, 45) and furthermore failed to allow the Railway Company credit for the full consideration parted with by it in the transactions.

No question is made or can be urged that bonds may not validly be issued in pledge for indebtedness, even at a discount. *William Frith v. So. Carolina L. & T. Co.*, 122 Fed. (4 *Cir. C. C. A.*) 569. *Atlantic Trust Co. v. Woodbridge Canal Co.*, 79 Fed. 501; 86 Fed. 975.

Upon foreclosure of the pledge the purchaser, even though the pledgee himself buys them in, may enforce them to their full face value regardless of the amount for which he took them in pledge.

Wade v. Railway Co., 149 *U. S.* 327; 37 L. Ed. 775.

Farmers L. & T. Co., v. Toledo R. Co. 54 Fed. 759.

If the pledgee still holds them in pledge without having foreclosed, he is nevertheless the owner thereof, and is entitled to prove ownership up to the face value of the bonds, although on distribution he may only receive dividends up to the amount of his pledge.

Jerome v. McCarter, 94 U. S. 734; 24 L. Ed. 136.

Duncome v. N. Y. R. Co., 84 *N. Y.* 190.
Hinckley v. Pfister 83 *Wis.* 64.

Where a corporation has pledged its bonds as collateral for a debt, it may afterwards assign its equity in such bonds to the pledgee, and the latter will thereby become absolute owner of the bonds.

Bibber-White Co., v. White River Valley E. Co. 175 Fed. 470.

Therefore the Court's decision recognizing the pledge of the 440 bonds was doubtless correct as far as it went. But as shown in the decision in *Thomas v. Brownsville Etc. R. Co., supra,* the question here is not one of technical pledge but of the consideration given for the fraudulently issued securities. In the case at bar the Railway Company agreed to part with $250,000 upon notes of the Power Company, in consideration of receiving $500,000 face value of the Power Company's First and Refunding mortgage bonds as security, and the privilege of exchanging consolidated bonds for up to $500,000 additional of said refunding bonds. The most bonds that it ever received was $718,000 face value, either under this transaction or the transaction of December 27th, with respect to the Bates & Rogers settlement. Therefore it holds less than it was entitled to under the original agreement of September 25th. Now if that agreement of September 25th was invalid for fraud, and therefore subject to be set aside, it was so fraudulent only to the excess of consideration received or agreed to be received over value given.

In such case, then, the Railway Company under the principle laid down in *Thomas v. Brownville etc. R. Co., supra*, and as a matter of equity and common fairness, is entitled to enforce the bonds to the extent of such value, and it makes no difference whether, as assumed by the Court, the Railway Company is the actor in the suit or not, for there, as here, the suit was to foreclose the mortgage securing the bonds, and decree of foreclosure was ordered for the amount of the value given.

Doubtless the trial Court, notwithstanding the language used indicating that it regarded the pledge as the primary element in the decision, intended to recognize this principle, but it failed utterly, in our view, to award the Railway Company the full value which it parted with for these bonds.

We think in view of the fact that the Railway Company acquired nothing under the Bates & Rogers transaction which it was not entitled to under the original transaction of September 25th, that all the elements of the consideration parted with by the Railway Company should be considered together, and that the Railway Company should have been awarded:

(1) The $250,000 cash advanced, with interest.

(2) The extent of the commitment to Bates & Rogers.

(3) The value of the second mortgage bonds.

(4) The value of the stock of the Railway Company.

The first and important element here is the $250,000 advanced by the Railway Company under the transaction of September 25th. The Court recognized this amount as having been advanced and for which it would under ordinary circumstances be entitled to credit (Supplemental decision *ante*, p. 44). But it subtracted from this apparent credit, the amount still due from Kissel, Kinnicutt & Company under the contract of September, 1911, viz., $140,000 and decreed reimbursement for only the difference, $110,000.

(c) *Neither the Railway Syndicate Nor the Railway Company Had Succeeded to the ~~Bonders'~~ Bankers' Obligation.*

We are unable to understand the legal reason for this deduction. Kissell, Kinnicutt & Company was not the Railway Company syndicate, nor was it the Railway Company. Neither the syndicate nor the Railway had at the time of this transaction assumed the obligation of Kissel, Kinnicutt & Company to purchase the second mortgage bonds of the Power Company. Our argument in this connection must necessarily be negative, and if we are in error in this statement the appellees should point out wherein the record shows the contrary.

The only place where this matter is discussed is on pages 195 to 197 inclusive of the Record, part of which is cited on pages 28 and 29 of the statement herein. On page 195 of the Record, after referring to the Bankers' contract of September, 1911, the witness states:

"Subsequently a syndicate was formed to take over the holdings of Kissel, Kinnicutt & Company in the Power Company, and in other properties which they had acquired and which later became the properties of the Railway Company."

Further, on the same page:

"The syndicate found itself owning a large interest in the Idaho-Oregon Company * * * The syndicate had two interests, thought it would be wise to turn over all of their interests in the Idaho-Oregon Company to the Idaho Railway Company which they did, taking securities of the same class from the Idaho Railway for securities of the Idaho-Oregon Company, which they turned into the Railway Company."

On pages 196 and 197, the membership of the syndicate is referred to, it being said:

"This syndicate was composed of a large number of individuals, perhaps fifty or one hundred * * * The syndicate was managed by Mr. Fuller's firm as syndicate managers. * * * His firm was probably the principal interest in the syndicate, although it was not the largest financial interest."

From a reading of this testimony it does not seem to us a legitimate inference that the syndicate had succeeded to Kissel, Kinnicutt & Company's liability to purchase these bonds of the Power Company. Certainly the syndicate could not have been sued for any default of Kissell, Kinnicutt & Company in this re-

spect. Doubtless as a practical matter, it was assumed that as consolidated bonds were received by Kissel, Kinnicutt & Company from the Power Company they would be turned in to the Railway Company, controlled by the syndicate, in exchange for the bonds of the Railway Company, and it is possible that the members of the syndicate were under obligation to Kissel, Kinnicutt & Company to contribute their share of the underwriting of the Power Company's bonds, but all this falls far short of establishing that the syndicate as a whole, or any members thereof, other than Kissel, Kinnicutt & Company, were legally or morally bound to purchase these bonds from the Power Company.

But if we assume that they were so bound still the Court's assumption is in no wise established. The Railway Company was an entirely distinct entity in law and in fact from the syndicate that controlled it. As stated in the testimony from which we have just quoted, stockholders of the Power Company were given the opportunity to exchange their securities in the Railway Company, the witness stating (Ante, p. 29): "A circular was sent out to all stockholders of record and a very large proportion of the stockholders so exchanged their stock" Furthermore, it is at least alleged by the interveners and may be admitted that the Messrs. Mainland had surrendered their large interests in the stock of the Power Company for stock in the Railway Company (ante p. 11).

It is not necessary, however, that the record affirm-

atively show that the Railway Company was not identical in fact with either the syndicate or Kissel, Kinnicutt & Company. If the Railway Company is to be deprived of a credit on the theory of any such identity in fact, regardless of legal identity, the record should clearly show such identity. It must be admitted that there was nowhere any liability of the Railway Company to assume this contract of the bankers to purchase the consolidated bonds. This being true, the right of the Railway Company to receive credit against these refunding bonds acquired by it under these transactions for the full amount paid or loaned to the Power Company cannot be offset by the existence of any unsatisfied liability of Kissel, Kinnicutt & Company, existing as of that date, to make additional advances on the consolidated bonds.

Assuming, however, the identity of the Railway Company and Kissel, Kinnicutt & Company, as far as this obligation was concerned, was not the substitution of the obligation to advance money upon refunding bonds, an entirely valid consideration for release of the obligation to purchase the consolidated bonds, regardless of questions of fraud which might enter into *other* aspects of the transaction?

We therefore contend that the Railway Company should have been allowed $250,000 instead of $110,000 against these bonds, and that such amount should have been allowed against the bonds as a whole instead of merely against 440 of the bonds.

(d) *Other Elements of Consideration.*

Other elements of the consideration parted with by the Railway Company will require but brief mention, as they are of minor importance. Second in importance, under the contract of December 27th, is the commitment of the Railway Company to Bates & Rogers for $20,000. True this was but a contingent liability, but if as assumed by the trial Court the consolidated bonds were worthless at the time, it was a liability that was sure to mature. Does the fact then of the present insolvency of the Railway Company deprive this commitment of its standing of consideration to the extent thereof for the bonds received, if any, under the transaction of December 27th? It doesn't appear, admitting the insolvency of the Railway Company, that Bates & Rogers Company can realize nothing upon its guaranty, and the Railway Company is clearly legally liable to Bates & Rogers for $20,000, if they seek to enforce such liability, whether it can be collected or not.

Second mortgage bonds may be admitted to be of no value upon liquidation of the Company in satisfaction of the claims of the first mortgage. It is not therefore to be assumed, however, that they were not of value in the fall of 1912. In any ordinary reorganization they would have been recognized. The Company's statement at the time showed that some interest was then being earned on them. That is, that there were some earnings over the amount required to satisfy the interest requirements on the first mortgage bonds. The earnings available for fixed charges

for the twelve months of 1912 were $237,430.16. (Record, p. 226). Approximately $3,000,000 of bonds including underlying issues prior to the consolidated bonds were outstanding (Record, p. 228). The interest charge at six per cent on these bonds was about $180,000.00. This would leave available for interest on the second mortgage bonds $57,000.00, or about 60 per cent of the interest requirements on the consolidated bonds then actually outstanding. True the probability of the Company continuing to earn this interest was, as we have previously stated, remote in view of the immediately approaching competition, but the bonds were not valueless. It was still possible that the competition might be eliminated, and the earnings preserved.

Finally the Court assumed the stock of the Railway Company given to Bates & Rogers to be of no value. There is no evidence as to what it was worth. There had been no public trading in it. The only evidence in the record is the financial statements shown on pages 213 to 218 inclusive, and the admission of its insolvency a year later, as stated on page 381. We do not urge that the Railway Company was in prosperous circumstances either in September or December, 1912, but we submit that it was by no means insolvent and its insolvency if imminent was primarily because of its large investment in Idaho-Oregon securities.

The principal point in pursuing this argument thus far, both as to the stock and to the bonds, is suggest the unfairness of looking at this transaction in

the light of the sequel and in attempting to judge the reasons and motives for the transaction at the time by their actual result, and in attempting now to adjust the equities as they would have worked out had these transactions not been had.

(e) *The Principle of Ratification.*

This argument leads logically to the question of ratification. The bondholders attacking this transaction are, as we have endeavored to show, standing in the shoes of the Company. But they seek to be excused from the operation of every legal principle which would have bound the company and its stockholders, had they sought to avoid the transaction. They make no objection until after there has been default in their mortgage as well as in the second mortgage, and the future of the Company has been determined by the events which have transpired. They do not offer or attempt to permit the restoration of the status, and they ignore all elements of estoppel. At the time these proceedings were commenced all opportunity of restoring the parties to the situation which they were in, in the fall of 1911 had passed. The transactions were entirely executed, the company had procured all it had bargained for, and the Railway Company could not be put in the situation that it would have been in had these transactions not taken place. In the fall of 1912 the Railway Company could at least have foreclosed its second mortgage upon the properties of the Power Company, and might have been able to reorganize them in such a way as would have preserved for itself

some equity in those properties had it proceeded promptly. By giving the company a new lease of life until the ~~new~~ first mortgage was in default, whether it acted wisely or not, it has lost all its standing under its second mortgage and is now refused practically all standing under the first. Under these circumstances we are satisfied that the Power Company, or its stockholders would be estopped, to rescind and repudiate these transactions. *Oil Company v. Marbury, supra; Robinson v. McCracken, supra; San Diego Co. v. Beach Co., supra.*

If, however, the Court considers that notwithstanding the impossibility of rescinding the transactions and restoring either the considerations given, or should they be restored, the status existing at the time, we earnestly submit that the Railway Company should be awarded a decree against these bonds for at least the money actually advanced—$250,000 and interest, and the extent of its commitment, $20,000—on the Bates & Rogers transaction, for which it is still liable. We are unable to see how, if every other point made is to be disregarded, or the application of the principles refused, the Railway Company should not be accorded this measure of relief.

V.

Errors in the Admission of Evidence.

But brief mention will be made of these. The questioned evidence as shown by specifications of error hereinbefore made is as to financial statements of the Railway and Power Companies. Evidence of

the condition of the Railway Company was admitted as stated in the specifications of error for the purpose of establishing a motive for the transactions. We do not think it tends so to do. Were the Railway Company in most prosperous condition its directors might have been especially eager to prevent that condition from being changed by the loss of value of second mortgage bonds. Were it already in a hopeless condition the same directors might have regarded the Company as not worth saving. Men who are confronted with a loss are naturally desirous of minimizing that loss and preventing it insofar as possible. We have never observed that the temptation is any less whether the man or the corporation is rich or poor, prosperous or otherwise. The errors assigned in this connection are numbers XXIII to XXVII inclusive.

With respect to specification No. XXVIII, we think that the evidence was doubtless competent upon some phases of the case. We do not think as contended by the Court that it tended to show the value of the Company's bonds upon the market, but the matter is not of importance.

Error XXIX relates to evidence of the financial history of the Power Company showing its gross earnings, operating expenses and net earnings for the years 1907 to 1912 inclusive, as shown by its auditors. We cannot see that this has any bearing on the case. Its only purpose must have been to prejudice the view of the Court as to the management of the Power Company by the so-called Railway inter-

ests by showing a more prosperous condition in earlier years. We have very largely explained this in the statement (*ante*, pp. 30, 32), and further by the evidence showing the liabilities of the Company and other financial data on pages 434 to 436 of the record. The allegations of the bill referring to these same matters as to the condition of the Power Company and of the Railway Company were not required to be answered by the defendant companies and no issues were made thereon. The reasons for unfavorable financial showings are various. Neither insolvency on the one hand nor prosperity on the other, nor good nor bad management can be inferred therefrom. Too many other elements enter into the situation. We think that the decision of the Court shows that these financial statements were prejudicial, and being without the issues as framed by the Court the Railway Company had little opportunity to meet them, and to have endeavored to meet them, would have required a mass of testimony as to conditions prevailing in the territory during the different years and comparative methods of bookkeeping, which could not in any way affect any relevant conclusion in the cause.

We do not contend, this being an equity suit, that the decree be reversed and the cause sent back for new trial on account of these errors, if they be such. We mention them simply if this Court deems them to be improper, to exclude them from consideration and to restrict the argument within limits.

This brief has grown to an excessive length for which we must ask the Court's indulgence in view of the importance of the questions involved, both in the legal principles and in the amount in controversy. Analyzed, as we have endeavored to analyze them, the facts are not complicated, nor are the principles contended for difficult of expression or comprehension. The practical situation which is here presented is one by no means of rare occurrence. A company apparently prosperous, but in structure fundamentally unsound, has conducted business for several years, but has become financially involved. An attempt is made by those then in charge of its affairs to meet the situation through a readjustment of securities, and to hold it intact until such readjustment is brought about. Bondholders who believed in the stability of their investment and were encouraged in that belief, as holders of security usually are up to the moment that its default is announced, feel that a fraud has been perpetrated upon them, or their situation would be different. Every expedient devised by those in charge of the Company for the purpose of preventing liquidation of its affairs is construed by the injured bondholders as a fraudulent device intended to rob them of their security. The estate becomes involved in litigation and its enforced liquidation makes reorganization and amicable adjustment between the interests involved impossible. Every act taken by those in charge of the Company's affairs is then construed, not in the light of what was sought to be accomplished; the considerations actuating those in charge with that end in

view are not considered, but an attempt is made to enforce rights and equities on the theory that the Company at the time these acts were taken, was, or should have been, in process of liquidation, and as though those acts were taken in contemplation of that step, instead of in contemplation of escaping such liquidation. Elements of time and possibility are not considered, and the charges of fraud are sustained upon the demonstrated proof of what has happened, instead of in the light of the conditions surrounding the transactions when had. The result is neither legally sound nor equitably just.

We submit that the decree should be reversed.

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